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IN THE U. S.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1965

No. 1149

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,
Petitioner,

vs.

D & L CONSTRUCTION CO. AND ASSOCIATES,
a Joint Venture,

AND

CONTINENTAL CASUALTY CO.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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CONTINENTAL CASUALTY CO.,
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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Petitioner National Union Fire Insurance Company of Pittsburgh, Pennsylvania, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit in the above entitled case.

OPINIONS BELOW

The opinion of the court of appeals is reported at 353 F.2d 169 and is reprinted in the Appendix, p. 5a, *infra*. The opinion of the United States District Court for the Western District of Missouri is reported at 234 F. Supp. 293 and is reprinted in the Appendix, p. 25a, *infra*. A supplemental opinion of the district court dealing with the allowance of pre-judgment interest and attorneys' fees is reported at 238 F. Supp. 815 and, while not germane to the issues presented by this petition, is reprinted in the Appendix, p. 73a, *infra*.

JURISDICTION

The judgment of the court of appeals was dated and entered November 18, 1965, Appendix, p. 22a, *infra*. Petitioner's timely petition for rehearing and motion for transfer to the court of appeals *en banc* were denied on December 27, 1965, Appendix, p. 24a, *infra*. Jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1). The jurisdiction of the district court was based on 28 U.S.C. § 1332 (a)(1). (R. 32)[1]

While the judgment below is not a final judgment since it remanded the case to the trial court for redetermination of damages, it did finally determine the issues on the merits of the case, and this Court has held that it has jurisdiction to review, and will review, the decision of the court of appeals where that decision is contrary to the decisions of this Court and those of other courts of appeals, and the decision is "fundamental to the further conduct of the case." *United States* v. *General Motors Corp.*, 323 U.S.

1. "R." refers to the Record certified to this Court by the court of appeals.

373, 377 (1944); *Land* v. *Dollar*, 330 U.S. 730, 734, n. 2 (1947); *Larson* v. *Domestic & Foreign Commerce Corp.*, 337 U.S. 682, 685, n. 3 (1948). That is precisely the situation in this case, since the court of appeals determined that federal law, not state law, governs the issues involved, and remand is for redetermination of damages "consistent with the views expressed in this opinion". Furthermore, this case involves an important and novel question of the application and scope of the rule of *Erie R. R. Co.* v. *Tompkins*, 304 U.S. 64 (1938), and petitioner's position, if sustained, would require reversal of the decision below.

This Court granted certiorari under similar circumstances in *Wallis* v. *Pan American Petroleum Corp. et al.*, No. 341, 34 U.S. L. Week 3102 (U.S. Oct. 11, 1965).

QUESTIONS PRESENTED

1. Whether, because a bonded subcontract relates to part of the work required of the prime contractor on a Capehart Act project, the rights and defenses of the subcontractor's surety shall be governed not by the laws of the appropriate state, as required by the constitutional precepts stated in *Erie R. R. Co.* v. *Tompkins* and further required by the Rules of Decision Act, but, instead, by federal judge-made law, and this despite the fact that the surety's bond is merely conventional and neither it nor the subcontract itself is executed under or required or regulated by any law of the United States.

2. Whether and to what extent "the federal interest inherent in Capehart projects" or the "need for uniformity" justifies the imposition of federal judge-made rules of decision in disputes arising out of agreements not governed by any law of the United States.

3. Whether, if federal law governs the rights of parties in disputes arising out of private agreements not governed

by any law of the United States, the federal courts should adopt state rules of decision rather than attempt to create novel and unprecedented federal rules of decision.

4. Whether the terms and conditions of prime contracts with the federal government or its agencies shall be deemed, as a matter of federal judge-made law, to be "incorporated by reference" in subcontracts with such prime contractor even though not so incorporated by the terms of such subcontracts.

5. Whether, in a dispute involving the interpretation of a conventional private surety agreement and the subcontract covered by such agreement, the federal courts may apply the law of a jurisdiction other than that selected by the parties to the subcontract.

STATUTES INVOLVED

This case involves the Rules of Decision Act, 28 U.S.C. § 1652 and 28 U.S.C. § 1352, the Miller Act, 40 U.S.C. §§ 270a and 270b and the Capehart Act, 40 U.S.C. § 1594. The pertinent provisions of these statutes are set forth in the Appendix, *infra*, pp. 1a-4a.

STATEMENT

This diversity case[2] arises out of the default of a subcontractor performing electrical work in the construction of military housing at Fort Leonard Wood, Missouri. The prime contract for this housing was awarded under the Capehart Act[3] to Respondent D & L Construction Com-

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2. Para. 2, Amended Pre-Trial Order (R. 32); Finding of Fact No. 1, 234 F. Supp. at 295.

3. Act of August 11, 1955, c. 783, Title IV, § 403, 69 Stat. 651, as amended by the Act of August 7, 1956, c. 1029, Title V, §§ 506(b)(d), 507, 70 Stat. 1110, 42 U.S.C. § 1594 *et seq.*

pany and Associates[4] a California joint venture. D & L's performance and payment bonds, the only bonds required or mentioned by the Capehart Act,[5] were furnished by Respondent Continental Casualty. The defaulting subcontractor, Mojave, has been adjudged bankrupt and was not a party to the appeal. Mojave's surety, National, is the petitioner here.

The action was originally instituted by Triangle, a materialman of Mojave, against D & L and Continental Casualty to recover the price of certain materials supplied by Triangle to Mojave for use in the performance of Mojave's subcontracts. Count II of Triangle's complaint sought recovery for the same items from National under its bonds. D & L and Continental Casualty thereupon asserted a cross-claim against National, likewise on the basis of its bonds written in Mojave's behalf, to recover from it not only sums for which they might be held liable to Triangle but also for amounts which had been or might be paid by them to satisfy other materialmen's claims and completion costs connected with Mojave's subcontracts.

Summary judgment was granted Triangle against D & L and Continental Casualty on Count I of its complaint, and this judgment was affirmed on appeal.[6] Count II of the

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4. Hereafter Respondents, D & L Construction Co. and Associates, and Continental Casualty Co., will be referred to as D & L and as Continental Casualty, respectively, and their joint pleadings, claims and contentions will be referred to as D & L's; National Union Fire Insurance Company of Pittsburgh, Pennsylvania, will be referred to as National; Mojave Electric Company will be referred to as Mojave; and Triangle Electric Supply Company will be referred to as Triangle.

5. 42 U.S.C. § 1594(a). The Capehart Act requirements respecting the prime contractor's payment and performance bonds reiterated existing requirements of the Miller Act. 49 Stat. 793, 40 U.S.C. § 270a(a)(1) and (2). See *United States* v. *Travelers Indemnity Co.*, 215 F. Supp. 455, 471-474 (W.D. Mo. 1963).

6. *D & L Constr. Co.* v. *Triangle Electric Supply Co.*, 332 F.2d 1009 (8th Cir. 1964).

complaint, against National, was dismissed pursuant to stipulation. Only the cross-claim of D & L and Continental Casualty against National thereafter remained for disposition. After extensive pre-trial proceedings and a short hearing before the court without a jury (R. 129-156), judgment was entered for D & L and Continental Casualty against National in the amount of $711,528.55 plus interest and costs (R. 199).

On National's appeal the court of appeals, affirming in part and reversing in part the decision of the trial court, held, inter alia, that federal law, not state law, governed the interpretation of National's obligation under its surety contract with Mojave; that, as a matter of federal law, the prime contract of D & L was incorporated in the subcontract of Mojave for purposes of determining National's obligations and defenses; and that the subcontract must be construed in light of the prime contract and the Heard and Miller Act cases. It is from this decision that National seeks the grant of a writ of certiorari.

The facts, most of which were stipulated to by the parties and set out in the Amended Pre-Trial Order (R. 32-42), may be summarized as follows: D & L contracted with the Federal Government on August 18, 1959, for the building of 700 units of military housing at Fort Leonard Wood. On the same day it executed with Mojave two separate subcontracts for the installation of electrical facilities called for by the prime contract. The subcontracts were drafted by D & L, in consultation with its legal counsel (R. 33).

Under the terms of Article IV(7) of the *prime contract,* D & L was entitled to monthly advance payments of the prime contract price on the basis of "the total of the purchase price or the estimated cost, whichever is less, of uninstalled acceptable materials suitably stored on the mortgaged property in a manner acceptable to the Con-

tracting Officer, plus the cost of the portions of the work acceptably completed, as approved by the Contracting Officer. . . ." The prime contract also provided that "the Contracting Officer or the mortgagee may require that the eligible builder [D & L] obtain and attach to each application for payment acknowledgments of payment to the date covered by the last advance from all subcontractors and materialmen dealing directly with the eligible builder [D & L]. . . ." (R. 42-44).

Under the terms of the *subcontracts* between Mojave and D & L, however, advance payments of the subcontract prices to Mojave were to be "at the rate of 90 per cent of all material and labor in place as shown on the following schedule: (*Payment to be based on actual progress*)[7] and payment will be made monthly as Contractor receives funds from the lender for same. . . ." (R. 9). Paragraph 9 of the subcontracts provided:

> "Subcontractor shall submit to the Contractor an application for each payment, and releases, receipts or other vouchers evidencing payment for materials and labor together with such additional evidence bearing on the right of the payment claimed as Contractor may direct." (R. 11).

Paragraph 54 of each of these subcontracts provided that they "shall be interpreted by the laws of the State of California" (R. 16).

Before its default Mojave did nothing toward the performance of its subcontracts with D & L other than to order, receive and store certain materials on the job site; it did not pay for them (R. 34). Although the subcontracts required that Mojave submit "a performance and payment bond with good and sufficient sureties . . . which

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7. Italicized portion typewritten into the printed subcontracts.

bond must be . . . submitted by August 29, 1959" (¶1, R. 8), applications for such bonds were not executed and dispatched by Mojave to agents for National until December 19, 1959 (R. 39). Copies of the electrical subcontracts between D & L and Mojave were submitted at the same time for National's use in considering Mojave's application (R. 39).

On October 15, 1959, however, Mojave had submitted to D & L two "subcontractor requisitions for funds" wherein it represented that it was entitled to progress payments for both subcontracts totaling $76,475.29. Mojave submitted no proof, other than its signed inventory, that the material inventories were actually stored on the job site as represented. No "releases, receipts or other vouchers" evidencing payment by Mojave to the materialmen furnishing the materials were presented by Mojave or required of it by D & L (R. 39). None of the materials were incorporated in any structure, and none of the actual installation required by either subcontract had begun.[8]

On November 16, 1959, D & L paid to Mojave the sum of $50,000 as a progress payment based solely on the documents submitted on October 15 (R. 38).

On November 15, 1959, Mojave submitted to D & L two further Subcontractor Requisitions for Funds wherein it represented that it was entitled to progress payments totaling $143,621 (R. 38). A Federal Housing Administration Project Inspection Report, obtained by D & L on November 20 and executed by an officer of the United States Army Corps of Engineers, indicated that as of that date the subcontracts were "0 per cent completed" (R. 39). A certificate appended thereto and executed by

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8. In fact, some of the material listed in those inventories as having been stored on the job site as of October 15, 1959, had not yet been shipped by the supplier (R. 38).

D & L's President indicated that the materials in question were stored on the job site and not "incorporated into the work".[9]

After Mojave was advised by officials of D & L that no further progress payments would be made to Mojave until acceptable evidence was produced that it had obtained the performance and payment bonds required by the subcontracts (R. 40), and after a telephone conversation on December 29, 1959, in which National's agent informed D & L that the bonds in question were in effect, D & L gave Mojave checks in the amounts of $68,373 and $25,248 representing payments purportedly due on the basis of the documents submitted by Mojave on November 15 and the project inspection report obtained by D & L on November 20 (R. 41).

The performance and payment bonds referred to above were delivered by National to D & L on or about January 13, 1960 (R. 42). Shortly thereafter Mojave defaulted under its subcontracts. Due notice of these defaults was given by D & L to National, and D & L demanded, by letter dated April 4, that "in accordance with the terms of Paragraph 4(a) of our two subcontracts with Mojave . . . you, as surety, immediately proceed with the work of said subcontractor" (R. 26). National declined thus to undertake completion of the subcontracts, and D & L thereafter engaged two other subcontractors to complete the work for a total price of $550,625.[10] After these subcontractors

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9. The Record contains extensive testimony by D & L's counsel, Fitzpatrick, as to what he conceived to be the "custom and practice" in financing Capehart projects permitting payments based on inventoried materials (R. 66-68). This evidence was seasonably objected to (R. 66, 67); nonetheless and in the face of the subcontracts' express provision governing payment, the trial court considered the testimony and adopted findings of fact based solely upon it (234 F. Supp. at 298).

10. Exhibits X and Y introduced at trial and omitted from the printed Record by stipulation. This figure was $20,625 more than the total of Mojave's subcontracts (R. 7-16).

likewise defaulted, D & L completed the interior and exterior electrical work with its own forces (R. 3).

D & L's amended cross-claim against National (R. 1-5) alleged execution of the subcontracts and subcontract bonds; Mojave's subsequent default by failure to pay materialmen and perform the construction called for by the subcontract; D & L's own completion of the project; the filing of claims against it by various materialmen furnishing goods to Mojave; D & L's resulting expenditure of sums for legal fees and expenses; and the making of demand upon National to remedy Mojave's default so as to reimburse D & L for its resulting damages.

In its amended answer (R. 18-21), National admitted execution of the bonds in question and Mojave's subsequent default. It went on to plead affirmatively that it was not liable under the bonds because (1) D & L had made premature and improper payments to its [National's] principal, Mojave, and (2) Mojave and D & L had fraudulently concealed from it, before execution of the bonds, the fact that such an improper payment had already been made and the circumstances surrounding it.

Stipulations of the parties on many factual matters were embodied in the Amended Pre-Trial Order entered April 13, 1964 (R. 32-42). The order set out the background facts given above and listed the various items of damage claimed.

After a short hearing without a jury (R. 129-156), the parties were directed to furnish their requested findings and conclusions (R. 156-198), with supporting briefs. Various contentions of the parties material to this petition and the trial court's rulings thereon as contained in its initial memorandum opinion, reported at 234 F. Supp. 293, may be summarized as follows:

Applicable Law. Throughout the proceedings below, D & L contended that the parties' rights were controlled

by the law of Missouri (where the subcontracts were to be performed), while National, relying on the stipulation for the applicability of California law in Paragraph 54 of the subcontracts (R. 16), asserted that California law should be applied. The trial court accepted neither of these positions and, instead, held that it must look to "the rules of decision developed under the Heard and Miller Act decisions." 234 F. Supp. at 305.

The trial court went one step further and concluded that "all substantive provisions of the Miller Act and the Capehart Act would be read into all performance and payment bonds required in connection with any government housing projects constructed under the Capehart Act" (234 F. Supp. 310), and that *American Cas. Co.* v. *Brezina Constr. Co.*, 295 F.2d 603 (8th Cir. 1961), required National's bonds to be construed "in light of" the prime contract and the Miller and Capehart Acts. 234 F. Supp. 310.[11]

The decision of the trial court suggested that this result was required by the uniformity which it sought "in connection with all the various problems growing out of the extensive Capehart litigation with which we have dealt," referring to *Travelers Indemnity* v. *Fine*, 215 F. Supp. at 466-475 (W.D. Mo. 1964). 234 F. Supp. at 309.

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11. Additional considerations which apparently led the trial court to reach the conclusion respecting incorporation of Miller and Capehart Act provisions as well as the terms of D & L's prime contract with the government into subcontract bonds included the following: (1) The bonds involved in the case made specific reference to the subcontracts between D & L and Mojave, and these subcontracts, in turn, showed "on their faces" that each subcontract was a part of the Capehart housing to be constructed at Fort Leonard Wood, (2) both subcontracts specifically incorporated all the "contract documents" of D & L's prime contract into each subcontract, (3) "the interdependence" of payment procedures of the prime contract and subcontracts, and (4) "all parties were bound to know the procedures for payments to the prime contractor as detailed in Article 4 of the prime contract" (234 F. Supp. 306-307).

Propriety of Payments to Mojave and Discharge of National Union. On this issue National contended that D & L's payments to Mojave had been improper because such payments were for "inventoried" materials and were not "based on actual progress" and for "material and labor in place" within the meaning of the provisions of the subcontract. National also objected to D & L's failure to require of Mojave, before payments were made, "releases, receipts or other vouchers evidencing payment [by Mojave] for materials and labor" as provided in paragraph 9 of the subcontracts. National's position was that under California law, a surety is exonerated *in toto* if the terms of the bonded contract are departed from in any material respect, regardless of whether there was any actual prejudice proved.

D & L's position was that the subcontracts were to be interpreted by Missouri law and were to be read in conjunction with its own prime contract with the government, which permitted payments to D & L for merely stockpiled materials. It also contended that the subcontract provision requiring releases and receipts was merely a discretionary matter which it could enforce if it was itself required to furnish those documents to the government or the lender. D & L contended that under the law of Missouri discharge could be, at most, *pro tanto,* and that the surety had the burden of proving actual prejudice and its extent.

The trial court disagreed with both D & L and National as to the question of state law. It held that federal law governed and that the subcontracts and bonds, when "read in light of" the prime contract and applicable federal statutes, authorized the payments in question. 234 F. Supp. 311-315.

On appeal the court of appeals affirmed the trial court's conclusions as to the applicable law, holding that the rules of decision "developed under the Heard and Miller Act

decisions" governed the case and that the surety on a subcontractor's bond, even though not required by any federal law and secured only at the request of the prime contractor, is held to the same rules of construction and contractual liability as the surety for the prime contractor. 353 F.2d at 171-172.[12] Consistent with its affirmance on the choice of law question and the issue of "incorporation" of the prime contract into the subcontract as a matter of federal law, the court of appeals also affirmed the trial court's conclusion that D & L's payments on the Mojave subcontract did not materially vary the payment provisions of that subcontract. 353 F.2d at 174-175.[13]

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12. The court of appeals expressly rejected National's contention that because the subcontracts between D & L and Mojave specifically stated "this contract shall be interpreted pursuant to the laws of the State of California," the obligation of the surety under the bonds in question was to be determined by the law of California. *Ibid.* The court of appeals correctly but inconsistently also ruled that National's rights and liabilities as surety must be measured by those of Mojave, its principal. 353 F.2d at 175.

13. It is true the court of appeals affirmed the trial court's "finding on conflicting evidence that National before executing the bonds had knowledge that such payments on inventory were customarily made on such projects and were in fact being made on this particular project, and that National had consented to such payments." There is, however, no evidence and no finding that National knew or consented to the payment of $50,000 to Mojave on November 16, 1959 (R. 38). 234 F. Supp. 301. Furthermore, the quoted "finding" is not effective to bar National's discharge under California law because it reaches only one of the two grounds on which National claimed discharge by reason of material variance of the subcontracts' terms. The finding refers only to National's claim for discharge based on D & L's material variance of "the material in place" provision of the subcontract (R. 9). The other and even more important ground for National's discharge is the subcontract provision requiring that Mojave submit to D & L an application for each payment for work in place, *together with releases, receipts or other vouchers evidencing payment by Mojave to its suppliers for materials and labor* (R. 11). There was no evidence, and neither court found, that National knew of or consented to the fact that D & L made payment to Mojave without proof of compliance with this provision. It is therefore clear that the result reached by the trial and appellate courts could have been reached only on the ground that, because federal and not state law governed this case, National was bound by the payment procedures provided in the prime contract with which it had nothing whatever to do.

Finally, and despite its holding that the applicable law was federal, the court of appeals held that National's liability under the subcontracts and bond for interest, including prejudgment interest, must be determined by state law. 353 F.2d at 176-177. Because of its ruling on the coverage of the bonds, the question of rights to allowance of attorneys' fees was not resolved, but the court indicated it would apply state law on this question also. 353 F.2d at 176. No reason was given for the application of "federal" law to determine National's defenses under its agreement with Mojave while state law was applied to determine National's liability under that same agreement for interest and attorneys' fees.

REASONS FOR GRANTING THE WRIT

I. The Importance of the Questions Presented.

There are nine important reasons why the writ should be granted in this case:

1. The decisions of the courts below that federal law is to be applied in this case conflict with this Court's decisions in *Erie R. R. Co.* v. *Tompkins*, 304 U.S. 64, 78 (1938); *Bernhardt* v. *Polygraphic Co.*, 350 U.S. 198, 202-204 (1955); *Bank of America* v. *Parnell*, 352 U.S. 29, 33-34 (1956); *Regents of the University System* v. *Carroll*, 338 U.S. 586, 594-602 (1950); and *United States* v. *Yazell*, 34 U.S.L.Week 4067 (1966).

2. By their application of federal law in this case, the decision of the courts below ignore or misapply the Rules of Decision Act, 28 U.S.C. § 1652 (1958).

3. This Court has already decided in this term *United States* v. *Yazell*, 34 U.S.L.Week 4067 (1966), a significant case dealing with an important aspect of the continuing problem of the interaction of federal and state laws in our complex federal system, and

applying state law in a case involving the direct rights of the United States. This petition for certiorari also presents questions which are similar to those before the Court in *Floyd A. Wallis* v. *Pan American Petro. Corp.*, No. 341, *cert. granted*, 34 U.S.L.Week 3102 (U.S. Oct. 11, 1965). In the present case, as in the *Yazell* and *Wallis* cases, the courts below decided an important question of the applicability of federal law and its scope, which has not been, but should be, settled by this Court.

4. The decisions of the courts below requiring the application of federal law and the incorporation of federal statutes and prime contracts into private non-statutory subcontracts and other arrangements only, at most, remotely connected with federal programs are of incalculable significance and will directly affect thousands of private transactions with no material bearing upon the administration of any federal statute or upon federal construction and procurement practices and will radically change the rules by which those transactions are planned and executed.

5. The decisions of the courts below conflict with those decisions of the federal courts in other circuits where state law was applied in the context of Government contract disputes and jurisdiction was based on diversity of citizenship. *Carruth* v. *Standard Acc. Ins. Co.*, 329 F.2d 690 (5th Cir. 1964); *Socony Vacuum Oil Co.* v. *Continental Cas. Co.*, 219 F.2d 645 (2d Cir. 1955); *Ogden Elec. Co.* v. *Engineers Ltd.*, 151 F.2d 657, 659 (10th Cir. 1945); *Glens Falls Indemnity Co.* v. *American Seating Co.*, 248 F.2d 846, 849 (9th Cir. 1957); *General Elec. Co.* v. *Southern Constr. Co.*, 229 F. Supp. 873, 876 (S.D. La. 1964). The decisions of the lower courts in this case also conflict with those decisions of other federal courts where jurisdiction was based on 28 U.S.C.A. § 1352 and the provisions of the Miller Act,[14] but where the courts nonetheless applied state

14. 49 Stat. 793, 40 U.S.C. § 270a *et seq.*

law because of the essentially private nature of the rights and contracts in dispute. *Continental Cas. Co.* v. *Schaefer*, 173 F.2d 5 (9th Cir.), *cert. denied*, 337 U.S. 940 (1949); *Sam Marci & Sons* v. *United States*, 313 F.2d 119, 124 at n. 1 (9th Cir. 1963); *Central Steel Erection Co.* v. *Will*, 304 F.2d 548, 554 (9th Cir. 1962); *Lichter* v. *Henke Constr. Co.*, 157 F.2d 13, 24 (8th Cir. 1946); *Blair* v. *Gregory-Hogan*, 147 F.2d 840, at 849 (8th Cir. 1945); *D. W. Winkelman* v. *Barr*, 178 F.2d 341, 343 (6th Cir. 1949); *Frommeyer* v. *L & R Constr. Co.*, 139 F. Supp. 579 (D. N.J. 1956); *Gillioz* v. *John Kerns Constr. Co.*, 50 F. Supp. 692 (E.D. Ark. 1943); *First Camden Nat. Bank* v. *Aetna Cas. & Sur. Co.*, 43 F. Supp. 596, 601 (D. N.J.), *aff'd*, 132 F.2d 114, 116 (3d Cir. 1942); *United States* v. *Rogers & Rogers*, 161 F. Supp. 132, 134-135 (S.D. Calif. 1958).

6. The fact that Congress over a long period of time has taken no action to change long-settled ways of handling problems as to applicable law, either in subcontract disputes in federal court merely because of diversity of citizenship or for suits actually filed under the Miller and Capehart Acts, further demonstrates the importance of the questions presented in this petition. "Congress has not seen fit to change the rules . . . fashioned in these cases"[15] despite its opportunity during the formulation of extensive legislation on Government building programs,[16] to overrule all of the cases cited above and to replace state law with uniform federal rules.

7. The decisions below that all terms of Miller and Capehart Act prime contracts are to be incorporated

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15. *Meyer* v. *United States*, 375 U.S. 233 at 239 (1963). See also *United States* v. *Standard Oil Co.*, 332 U.S. 301 at 310 (1947).

16. *E.g.*, 46 Stat. 1494 (1931) as amended, 40 U.S.C. § 276a (1958) (regulation of wages); 74 Stat. 740 (1960), 41 U.S.C. §§ 51-54 (Supp. II, 1961) ("anti-kickback" statute); 65 Stat. 7 (1951), 50 U.S.C. App. Secs. 1211-12 (1958) (renegotiation of contracts and subcontracts); 10 U.S.C. § 2301 (1958), 67 Stat. 232 (1953), as amended, 15 U.S.C. §§ 637-38 (1958); 69 Stat. 580 (1955), 50 U.S.C. App. Sec. 2151 (1958).

into subcontracts thereunder, and that the subcontracts are to be construed according to the Miller and Capehart Acts, directly conflict with the decision of this Court in *Guerini Stone Co.* v. *Carlin Constr. Co.*, 240 U.S. 264 (1915).

8. The failure of the courts below to consider the constitutional and statutory implications of their decisions respecting the applicable law and its scope, and their rejection of the parties' choice of California law, demonstrate that they have so far departed from the accepted and usual course of judicial proceedings, and that the court of appeals has so far sanctioned such departure by the trial court, as to call for an exercise of this Court's power of supervision to correct instances of the improper administration of governing legal rules. Such failure by the lower courts to follow the standards enunciated in *Erie R. R. Co.* v. *Tompkins, supra*, p. 14; *Bank of America* v. *Parnell*, 352 U.S. 29 (1956), and *Guerini Stone Co.* v. *Carlin Constr. Co., supra*, or to adhere to the statutory command of the Rules of Decision Act, fully justifies the grant of certiorari to correct a serious instance of improper administration of the *Erie* rule and to prevent that rule's erosion. See *Rogers* v. *Missouri Pacific R. R. Co.*, 352 U.S. 500 at 509 (1957).

9. The lower courts relied on "the federal interest inherent in Capehart projects" and the "need for uniformity", to justify their choice of law. They did so, however, without making the careful analysis of any such "federal interest," which is required by such decisions as *Bank of America* v. *Parnell, supra*, and *Regents of the University System* v. *Carroll, supra*. This failure again demonstrates that the lower courts here have so far departed from the accepted and usual course of judicial proceedings, and that the court of appeals has so far sanctioned such a departure by the trial court, as to call for an exercise of this Court's power of supervision to correct these instances of abuse of the governing legal standard. *Rogers* v. *Missouri Pacific R. R. Co., supra*.

II. As to Whether the Applicable Law Is State or Federal.

A. The decisions of the courts below conflict with decisions of this Court and fail to follow the Rules of Decision Act.

The decisions below are wrong and they are wrong in a way that is destructive of the constitutional principles which control "the interaction of federal and state laws in our complex federal system". *United States* v. *Yazell*, 34 U.S. L.Week 4067 (1966).

Specifically this case raises questions fundamental to the application of the constitutional principle stated by Mr. Justice Brandeis in *Erie R. R. Co.* v. *Tompkins*, 304 U.S. 64, 78 (1938), that the federal courts are without power to declare substantive rules of common law in any case, except in matters governed by the federal Constitution or by Acts of Congress. This case raises equally important questions respecting the duty of the lower federal courts to obey the command of the Rules of Decision Act, 28 U.S.C. § 1652 (1958), that "the laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States in cases where they apply." The decisions of the courts below are exceptional for their stated conclusion that federal law must be created and applied to govern the private rights of private parties in any way connected with a government housing project despite the lack of a federal statutory or other federal interest in the parties or their rights *inter sese*, and for their unstated conclusion that state law may be ignored in such situations.

Originally this case involved only one issue: Who is to bear the burden of Mojave's default—D & L, the prime contractor and Continental Casualty, its surety, or National, Mojave's surety. All of the materialmen, the persons whom the Miller and Capehart Acts were designed to protect, have

been paid. The Fort Leonard Wood structures have been built and paid for, and the federal government cannot be affected one whit whether D & L's or Mojave's surety shoulders the loss arising out of Mojave's default. Both the federal government and all materialmen and laborers at Fort Leonard Wood were completely and effectively protected by the prime contract bonds. Only those bonds were required by federal statute, because only those bonds involved federal interests. Mojave's subcontract bonds were required by D & L, not by the federal government, and were required for the sole purpose of protecting D & L. D & L lost this protection and National was freed of any obligations to D & L because, under the law of California, D & L's failure to discharge its duties toward its surety and to comply with the payment procedures in its own subcontracts discharged National *in toto*.[17]

The trial court acknowledged that the subcontract bonds in dispute are neither Miller Act nor Capehart Act bonds—*i.e.*, that they were not required by either statute. 234 F. Supp. at 306. In any case, this Court has expressly ruled that the Miller Act was not intended to change those equitable suretyship principles "so deeply embedded in our commercial practice, our economy and our law." *Pearlman* v. *Reliance Ins. Co.*, 371 U.S. 132, 140 (1962).

It is noteworthy, moreover, that this is a diversity action and nothing more[18] (though "it is the *source* of the right sued upon, and not the ground on which federal jurisdiction over the case is founded, which determines the governing

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17. California Civil Code § 2819 and § 1787 (1962); *First Congregational Church* v. *Lowrey*, 175 Cal. 124, 165 Pac. 440 (1917); *Pacific Coast Engineering Co.* v. *Detroit Fid. & Sur. Co.*, 214 Cal. 384, 5 P.2d 888 (1931); *Glenn County* v. *Jones*, 146 Cal. 518, 80 Pac. 695 (1905).

18. Para. 2, Amended Pre-Trial Order, R. 32; Finding of Fact No. 1, 234 F. Supp. at 295.

law").[19] The bonds sued upon were not "executed under any law of the United States" (28 U.S.C. Sec. 1352), and the case does not involve any issue "arising under the Constitution, laws or treaties of the United States" (28 U.S.C. Sec. 1331). There is, therefore, no basis for federal jurisdiction in this case other than diversity of citizenship. Except for the accident of diversity, D & L would have been required to initiate its action against National in a state court. *Gully* v. *First Nat. Bank*, 299 U.S. 109 (1936). As in *Trimount Dredging Co.* v. *United States Fid. & Guar. Co.*, 166 Md. 556, 171 Atl. 700 (1934), a suit by a subcontractor involved in a Heard Act project brought in state court because of lack of diversity of citizenship between the parties, the law to be applied would be that of the state.

On this record and under the Court's earlier holding in *Klaxon Co.* v. *Stentor Electric Mfg. Co.*, 313 U.S. 487 (1941), the trial court should have applied the conflict of laws rule of Missouri to determine the state law governing the substantive rights and obligations of the parties.[20] Missouri conflicts law,[21] when considered with the express provision of the subcontract requiring the application of California law,[22] should have led the trial court (and the court of appeals) to proceed in a conventional way with the application of California law, and to resolve the basic question as to who was to bear the burden of Mojave's default.

Neither court, however, heeded the requirements of *Erie* and its progeny, or the Rules of Decision Act, but instead

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19. *Maternally Yours, Inc.* v. *Your Maternity Shop, Inc.*, 234 F.2d 538, 540-541, n. 1 (2d Cir. 1956).

20. The court of appeals had so held in a Miller Act case, *Lichter* v. *Henke Const. Co.*, 157 F.2d 13 (8th Cir. 1946).

21. *Fidelity Loan Securities Co.* v. *Moore*, 280 Mo. 315, 217 S.W. 286 (1919).

22. *Mass. Bonding & Ins. Co.* v. *Feutz*, 182 F.2d 752, 756-757 (8th Cir. 1950).

created out of whole cloth a federal rule that is totally novel and far-reaching. The rule is even more than these things, however, for it refers to no established state rules of contract bond interpretation; it remains indefinite and potentially without limit in its application to cases and lawsuits of this kind. This case, therefore, represents exactly that kind of judicial lawmaking which, as Mr. Justice Brandeis concluded, is without the sanction of the Constitution or the Acts of Congress.

Because the courts below did not follow the clear commands of *Erie* or the Rules of Decision Act, this case reintroduces or compounds the uncertainty which *Erie* sought to eliminate. As the court said in *Continental Cas. Co.* v. *Schaefer*, 173 F.2d 5, at 8 (9th Cir.), *cert. denied*, 337 U.S. 940 (1949):

> "The rights and liabilities of the parties under the subcontract should not depend on the choice of forum sought to enforce those rights."

Yet that is precisely the result which will follow from the decisions here: The rights and liabilities of the parties will depend on the choice of forum in which those rights are adjudicated. This case is a perfect example of the significance of the parties' choice of forum. Had D & L sued National in state court, the law of California or that of Missouri would have been applied. Neither party claimed to the contrary. Under those laws National's obligations were limited to the terms and conditions of the subcontract and bond, and D & L's departures from the payment provisions in the subcontract would have effected a discharge of National *in toto* or *pro tanto*. Because the lawsuit was tried in federal court, however, National's obligations were construed "in light of" the prime contract and decisions under the Heard, Miller and Capehart Acts, with

the unexpected result that National became liable under its bond. The courts below were oblivious to these considerations. Neither the court of appeals nor the trial court referred at any point to *Erie* or to the Rules of Decision Act;[23] neither court considered the evil of forum shopping which their opinions resurrect.

The significance of the decision that federal law should be applied to the issues arising between these parties cannot be overstated. Over 1,000 cases arising under the Miller Act[24] have been filed in the United States District Courts each year between 1961 and 1964, inclusive.[25] The figures supplied by the Administrative Office of the United States Courts do not show the number of diversity cases involving Miller Act and Capehart Act subcontractors or suppliers; nor do they show the number of state cases involving such

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23. As the trial court recognized, its choice of federal laws came as a complete surprise to all parties. 234 F. Supp. at 310. The entire choice of law question was exhaustively briefed on appeal, however, at pp. 26-48 of National's initial brief. Furthermore the principal thrust of National's petition for rehearing and motion for transfer to the court of appeals *en banc* was that the choice of law decisions of the trial court and the court of appeals were erroneous under *Erie* and the Rules of Decision Act and in conflict with the decisions of other federal courts.

24. Although there are no statistics as to the number of contract bond cases filed in the various state and federal courts, Miller Act cases raise identical questions respecting the governing law.

25. During the fiscal year ending June 30, 1964, 1,053 actions under the Miller Act were commenced in the United States District Courts. Table C-2, p. 218, Annual Report of the Director of the Administrative Office of the United States Courts (1964). There were 1,092 Miller Act cases commenced during the fiscal year ending June 30, 1963. Table C-2, p. 198, Report of the Proceedings of the Judicial Conference of the United States (1963). During the fiscal year 1962 there were 1,000 Miller Act cases commenced. Table C-2, p. 196, Annual Report of the Director of the Administrative Office of the United States Courts (1962). 1,333 cases under the Miller Act were commenced in the fiscal year 1961. Table C-2, p. 238, Annual Report of the Director of the Administrative Office of the United States Courts (1961).

issues.[26] The decisions below would require the application

26. A showing of the number of cases actually litigated would, of course, only scratch the surface. The uncertainty created by the decisions of the courts below would be felt in an even greater number of procurement transactions where the federal government was "involved". As the Subcommittee on Federal Procurement and Regulation reported:

> "It is impossible to portray the scope of Federal procurement. The Department of Defense alone issues some 10 million contract actions annually. The estimated dollar range of Federal procurement obligations is shown by Budget Bureau statistics as follows for the fiscal year 1965:
>
> | | *Billions* |
> |---|---|
> | Contractual services and supplies: | |
> | Travel and transportation of persons | $ 1.262 |
> | Transportation of things | 2.989 |
> | Rent, communications, and utilities | 2.258 |
> | Printing and reproduction | .266 |
> | Other services | 20.441 |
> | Services of other agencies | .846 |
> | Supplies and materials | 20.896 |
> | Total | 48.959 |
> | Acquisition of capital assets: | |
> | Equipment | 14.971 |
> | Lands and structures | 4.574 |
> | Investments and loans | 9.912 |
> | Total | 29.457 |
> | Grand total | 78.416 |
>
> In addition to such annual outlays are the estimated Federal real and personal property holdings, generally computed at acquisition cost, as of June 30, 1964:
>
> | | *Billions* |
> |---|---|
> | Personalty | $230 |
> | Realty | 94 |
>
> It is obvious that the questions of how the functions of procurement, transportation, storage, issuance, and disposal are done—and where, when, and by whom—vitally affect our economy. These activities have great impact even on an economy with an anticipated gross national product of $660 billion in 1965."

Staff of the Subcommittee on Federal Procurement and Regulation of the Joint Economic Committee Congress of the United States, 89th Cong., 1st Sess., Report on the Economic Impact of Federal Procurement 1-2 (Joint Comm. Print 1965).

In Missouri alone, there were military procurement actions in 1964 totaling $1,349,071,000. Staff of Subcommittee on Federal Procurement and Regulation, Joint Economic Committee, 89th Cong., 1st Sess., Background Material on Economic Impact of Federal Procurement 10-11 (Joint Comm. Print 1965).

of federal law to determine the outcome of all such disputes between private parties to a transaction somehow touched by the federal presence, no matter how remotely. The decisions below thus greatly extend the federal presence and thrust it into otherwise private transactions, causing surprise and confusion to all concerned. The most immediate practical effect of the decisions below is to render uncertain the law by which any transaction between private parties incidentally involved in a public works project is to be governed, and to recreate and revive the pernicious situation which *Erie* was intended to eliminate.

Consistent with their indifference to *Erie* and the Rules of Decision Act, the opinions of the courts below fail to mention or consider the conflict of their determinations with this Court's decisions in *Bank of America* v. *Parnell*, 352 U.S. 29, 33-34 (1956), and *Regents of the University System* v. *Carroll*, 338 U.S. 586, 594-602. As recently as January 14, 1966, in *United States* v. *Yazell*, *supra*, p. 14, this Court said:

> "None of the cases in which this Court has devised and applied a federal principle of law superseding state law involved an issue arising from an individually negotiated contract." 34 U.S.L.Week at 4070.

If anything, the present case is *a fortiori* to *Yazell*. Here, unlike that case, there is not the unqualified federal interest there must be when the United States sues to protect its rights in a transaction and under an agreement to which it is a party. This case is precisely one of those which this Court distinguished in *Yazell*: The issue of National's exoneration and discharge from liability under its subcontract bond arises from an individually negotiated surety agreement between National and Mojave, the subcontractor. That issue can only properly be decided by the analysis and application of state law.

National's petition herein also presents questions which are similar to those now before the Court in *Floyd A. Wallis* v. *Pan American Petro. Corp.*, No. 341, *cert. granted*, 34 U.S.L. Week 3102 (U.S. Oct. 11, 1965). The issue in the *Wallis* case is whether state or federal law governs the adjudication of a dispute among three private individuals over their respective interests in an oil and gas lease issued by the United States under the Mineral Leasing Act of 1920,[27] and whether Louisiana's refusal to recognize estoppel as a basis for obtaining an interest in a mineral lease bars one party's claim. Reversing the decision of the trial court which followed Louisiana law [200 F. Supp. 468 (E.D. La. 1961)], the court of appeals held that in light of the "comprehensive scheme of federal regulation" embodied in the Mineral Leasing Act, the "interest of the United States [was] directly affected" by the controversy between the parties so as to make federal rather than state law applicable in determining the merits of the claims. 344 F.2d 432; *opinion on rehearing*, 344 F.2d 439, 441, 442 (5th Cir. 1965). In the present case, the courts below incorrectly decided important questions of the applicability of federal law and the scope of that law in an expanding area of civil litigation. Those questions are surely as important as those considered in the *Yazell* and *Wallis* cases and they have not been, but should be, settled by this Court.

B. The decisions of the courts below conflict with the decisions of lower federal courts in other circuits and with decisions in the Eighth Circuit itself.

The decision of the court of appeals is in conflict with the decisions of the courts of appeals in the Second, Fifth, Sixth, Ninth and Tenth Circuits; it also appears to be in conflict with other decisions in the Eighth Circuit itself. All

27. 41 Stat. 437, as amended, 30 U.S.C. § 181 *et seq.*

of these decisions, in varying kinds of private disputes between private parties, not even as remote from some "federal interest" as is the controversy in this case, are unanimous in holding that suits between private parties to subcontracts for work on government jobs are within the *Erie* rule and, therefore, that state law must be applied. These decisions fall into two catagories: First, there are diversity cases, like the case at bar, where there is or should be no dispute about the application of the *Erie* doctrine; second, there are other cases where the jurisdiction of the court was dependent upon 28 U.S.C. § 1352 and the provisions of the Miller Act, but where the court nonetheless applied state law because of the essentially private nature of the rights and contracts in dispute.

The most emphatic and helpful of those decisions in the first catagory, *i.e.*, diversity cases, are *Carruth* v. *Standard Acc. Ins. Co.*, 329 F.2d 690, 691-692 (5th Cir. 1964), and *Socony Vacuum Oil Co.* v. *Continental Cas. Co.*, 219 F.2d 645 (2d Cir. 1955). *Carruth* was an action on a subcontractor's bond where the issue was whether the bond covered rental on heavy equipment left on the job by a sub-subcontractor when it abandoned the project, and thereafter used by the subcontractor to complete the work. The trial court held that the bond did not cover the rental, even though the application of "federal law" would have required a different conclusion. The court of appeals affirmed, holding that state law controlled because "the payment bond in question was private or conventional, as distinguished from statutory, and . . . the parties were therefore at liberty to make the bond as broad or as narrow as they pleased and to have it cover anything they specify." 329 F.2d at 691-692.

In the *Socony Vacuum* case plaintiff was a materialman of the subcontractor who failed to perfect his rights against the surety on the prime contractor's payment bond with-

in the time limit provided in the Miller Act, 40 U.S.C.A. § 270b(a). Plaintiff therefore filed an action in the United States District Court to recover from the subcontractor's surety. Reversing the trial court's dismissal of plaintiff's complaint, the court of appeals held that, notwithstanding plaintiff's failure to file a timely claim under federal law against the prime contractor's surety, it was not precluded from recovering the amount of its claim from the subcontractor's surety. On the choice of law question, the court said there was nothing in the record to show the parties to the bond contemplated that it was to be interpreted or governed by the law of a particular state, and accordingly, under *Erie R. R. Co.* v. *Tompkins*, the problem was determined by the law of Vermont. 219 F.2d at 647.[28]

Even cases filed under the Miller Act recognize that state law should be applied to essentially private rights not dependent on the construction of federal statutes and not involving the United States as a party, although the federal court acquired jurisdiction by virtue of a statutory jurisdictional grant.[29]

The clear conflict between the decisions below and the decisions of other courts of appeals serves to emphasize the importance of the conflict between decisions within the Eighth Circuit itself. Thus the decisions in the instant

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28. *Accord, Ogden Elec. Co.* v. *Engineers, Ltd.*, 151 F.2d 657, 659 (10th Cir. 1945); *Glens Falls Indem. Co.* v. *American Seating Co.*, 248 F.2d 846, 849 (9th Cir. 1957); *General Elec. Co.* v. *Southern Constr. Co.*, 229 F. Supp. 873, 876 (W.D. La. 1964).

29. *E.g., Lichter* v. *Henke Constr. Co.*, 157 F.2d 13 (8th Cir. 1946); *Continental Cas. Co.* v. *Schaefer*, 173 F.2d 5 (9th Cir.), *cert. denied*, 337 U.S. 940 (1949); *D. W. Winkelman* v. *Barr*, 178 F.2d 341, 343 (6th Cir. 1949); *Frommeyer* v. *L & R Constr. Co.*, 139 F. Supp. 579 (D. N.J. 1956); *Gillioz* v. *John Kerns Constr. Co.*, 50 F. Supp. 692 (E.D. Ark. 1943); *Sam Marci & Sons* v. *United States*, 313 F.2d 119, 124 at n. 1 (9th Cir. 1963); *Central Steel Erection Co.* v. *Will*, 304 F.2d 548, 554 (9th Cir. 1962).

case conflict with those in *Lichter* v. *Henke Constr. Co.*, 157 F.2d 13, 24 (8th Cir. 1946) and *Blair* v. *Gregory-Hogan*, 147 F.2d 840 at 849 (8th Cir. 1945). State law was applied to resolve disputed issues in both *Lichter* and *Blair* even though those cases were brought under the Miller Act. Yet neither of the courts below referred to or distinguished *Lichter* and *Blair* in their opinions.

Prior to the decision in the present case, but subsequent to the *Lichter* and *Blair* decisions, the trial court had decided *United States* v. *Travelers Indem. Co.*, 215 F. Supp. 455 (W.D. Mo. 1963), a Miller Act case arising under 28 U.S.C. § 1352. There it stated: "the rules of decision that will be applied to the factual situations involved in the various cases [meaning all of the Capehart Act cases pending in the Southern Division of the Western District of Missouri] will be the rules of decision developed under the Heard and Miller Act decisions," and state law was held to be inapplicable. 215 F. Supp. at 474. This holding was adopted by the Eighth Circuit Court of Appeals in *D & L Construction Co.* v. *Triangle Electric Supply Co.*, 332 F.2d 1009, 1012 (8th Cir. 1964).[30] The correctness of these conclusions is only indirectly before the Court as it considers this petition since both the trial court and the court of appeals were considering, in the cited cases, problems of liability under *prime contract bonds* required by an act of the United States and jurisdiction was based on Section 1352 of Title 28. That is not the case here: The bonds now in dispute were not required by any act of the United States and are, for lack of a better term, "private" bonds. Notwithstanding this important distinction, there are sound reasons for also doubting, in the context of "federal ques-

30. The decision to apply an undefined judge-made federal law in all cases "involved" in "Capehart and Miller Act litigation" did not achieve doctrinal absoluteness in the Eighth Circuit, however, until the present case was decided.

tion" litigation, the validity of the rule of decision adopted by the courts below in the *Triangle* and *Traveler's* cases, *supra*. See, *e.g.*, *Lichter* v. *Henke Constr. Co.*, 157 F.2d 13 (8th Cir. 1946); *Continental Cas. Co.* v. *Schaefer*, 173 F.2d 5 (9th Cir.), *cert. denied*, 337 U.S. 940 (1949); *D. W. Winkelman* v. *Barr*, 178 F.2d 341, 343 (6th Cir. 1949); *Sam Marci & Sons* v. *United States*, 313 F.2d 119, 124 at n. 1 (9th Cir. 1963); *Central Steel Erection Co.* v. *Will*, 304 F.2d 548, 554 (9th Cir. 1962).

This reference to the development of the Eighth Circuit's rule of decision is to show that the lower courts here have deviated, not only from standards followed by other courts of appeals in both federal question and diversity cases, but also from the Eighth Circuit's own standards and rules governing the application of state law, and that this deviation has become more significant and more destructive of the true and original standard as each new case is decided. This snowball effect which can be observed in the opinions of the court of appeals requires prompt correction by this Court. *Dickinson* v. *Petroleum Conversion Corp.*, 338 U.S. 507, 508 (1950).

The startling inattention of the court of appeals to its own rules of decision as well as to those of this Court becomes altogether shocking when considered with the fact that the courts below appear to apply a given rule of decision in an arbitrary and capricious way: While "federal law" was selected for determining some of petitioner's rights and duties under the bond and subcontracts, state law was selected for determining its other rights and duties under the same bond and subcontracts. 353 F.2d at 176-177; 234 F. Supp. at 818-819. How, under these circumstances, are litigants to know what law applies to their transaction or to any part of it?

Surely the *Erie* rules cannot be interpreted to permit so grotesque a result as that achieved by the lower courts here. The lesson of *Rogers* v. *Missouri Pacific Ry.*, 352 U.S. 500, 510 (1957), should therefore be applied: Because the lower federal courts in this case have persistently and arbitrarily misapplied the governing legal standard, "special and important reasons for the grant of certiorari . . . are certainly present."

C. As to the "federal interest" in subcontracts or subcontract bonds justifying the imposition of a uniform federal rule.

As already stated, the sole reason for applying federal law to the issues raised in the case appears to be "the federal interest inherent in Capehart projects" (353 F.2d at 172), or "uniformity in connection with all of the various problems growing out of the extensive Capehart litigation" (234 F. Supp. at 309). At neither the trial nor appellate level is this "federal interest" or the reasons for "uniformity" in a case of this sort more specifically described. In view of the fact that it furnishes the occasion for an outright departure from *Erie*, the supposed federal interests at stake deserve a more careful definition and critical evaluation.

National submits that in fact the federal government has *no* interest, direct or remote, in the outcome of this litigation. Since all of the materialmen in question have been paid, the policy of the Miller and Capehart Acts to protect materialmen on government contracts is not involved. Since also the Fort Leonard Wood structures have been built and paid for, the federal government has no interest in the dispute of D & L and its surety, Continental Casualty, with National, Mojave's surety, as to who should bear the loss arising out of Mojave's default. There is "no decisional or doctrinal justification for applying

judge-made federal common law to a private dog-fight in which the federal government's interest, if any, seems . . . to be that of a bored spectator."[31] Mere uniformity in and of itself is not sufficient to justify the disregard of *Erie* and the imposition of federal rules of decision. *Bank of America* v. *Parnell*, 352 U.S. 29, 33-34 (1956).[32] Indeed the Solicitor General's brief before the Supreme Court in *Wallis* v. *Pan American Petro. Corp., supra*, vindicates National's position. There the Solicitor General argued that the rights of the litigants could properly be left to determination under principles of state law because the claims in that case were not based upon any alleged violation of a federal statute, regulation or order, the validity of the lease of the United States under the Mineral Leasing Act of 1920 was not in issue, the United States itself was not a party to the transaction in suit, and the application of state law would not undermine some federal interest or policy drawn from the Mineral Leasing Act of 1920.[33] Likewise the rights of the litigants here can be and should be left to determination under principles of state law because the claims are not based upon any violation of federal statute, regulation or order, the validity of the subcontracts and bond under the Capehart Act is not in issue, the United States is not a party to the transaction in suit and the application of state law would not undermine some federal interest or policy drawn from the Capehart or Miller Acts.

Finally, it must be remembered that Congress has had ample opportunity, during the formulation of extensive

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31. Dissent of Judge Wisdom in *McKenna* v. *Wallis*, 344 F.2d 432, *on rehearing*, 344 F.2d 439 at 452, *cert. granted*, 34 U.S.L.Week 3102 (U.S. Oct. 11, 1965).

32. See also *McKenna* v. *Wallis*, 344 F.2d 432, *on rehearing*, 344 F.2d 439 at 452 (5th Cir. 1965) (dissent).

33. Memorandum for the United States as Amicus Curiae, pp. 7-8, 10-14; *Wallis* v. *Pan-American Petro. Corp., supra.*

legislation on government building programs[34] to overrule all the cases cited above and to supplant state law with uniform federal rules. It has not done so, either as to subcontract disputes in federal court merely because of diversity in the parties' citizenship, or in suits actually filed under the Miller and Capehart Acts.[35] This fact alone, when considered with the substantial practical problems of limiting the reach of such federal rules, demonstrates the unsoundness, even carelessness, of the decisions below.

III. As to the Incorporation, As a Matter of Federal Law, of the Prime Contract into the Subcontract.

The court of appeals' ruling in *American Cas. Co.* v. *Brezina Constr. Co.*, 295 F.2d 603 (8th Cir. 1961), was regarded as pivotal in opinions written at the trial and appellate levels. *Brezina* was apparently construed as establishing two distinct propositions: (1) federal (not state) law is to be applied not only to prime contract bonds required by federal statute but also to private subcontract bonds issued solely at request of the prime contractor (234 F. Supp. at 308-309 and 353 F.2d at 172), and (2) as a matter of federal law, all terms of Miller and Capehart Act prime contracts are to be incorporated into the subcontracts and a subcontract bond must be viewed and interpreted in light of the provisions of the subcontract and the general contract (234 F. Supp. at 308 and 353 F.2d at 172).

Aside from the fact that *Brezina* hardly stands for either of the propositions for which it was cited,[36] even if it did,

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34. See n. 16, *supra*, p. 16.

35. See *Meyer* v. *United States*, 375 U.S. 233, 239 (1963); *United States* v. *Standard Oil Co.*, 332 U.S. 301, 310 (1947).

36. Since the subcontract in *Brezina* explicitly incorporated within it by reference *all* of the provisions of the prime contract and specifically committed the subcontractor to be bound to the prime contractor by the terms of the prime contract. See 295 F.2d 607, n. 7.

serious departures from the rule of construction announced in *Guerini Stone Co.* v. *Carlin Constr. Co.*, 240 U.S. 264 (1915), are indicated.

The true rule concerning the relationship between the prime and subcontracts is that employed by this Court in the *Guerini* case. That case arose out of difficulties encountered during the construction of the United States Post Office in San Juan, Puerto Rico. Carlin, the prime contractor on the job, subcontracted to Guerini certain of the concrete and granite work. Carlin's prime contract with the government provided that the latter had the right to suspend work on the project whenever it might be "necessary for the purposes or advantage of the work," and that the government would not be responsible to Carlin for any damages which might accrue because of such a delay. The General Conditions attached to the prime contract contained a similar provision. Guerini's subcontract, however, said nothing about delays caused by the government. Instead, it provided that Carlin would provide materials to Guerini "in such a manner as not to delay the material progress of the work." After certain delays Guerini notified Carlin that it regarded the subcontract as having been breached and thereafter filed suit to recover its anticipated profits and damages.

Although Carlin made some attempt to controvert the facts alleged by Guerini, its primary defense bore striking resemblance to that advanced by D & L in the case at bar and sustained by the courts below. It pointed out that its own contract with the government allowed the latter to halt work on the project without responsibility for damages caused by the delay. Guerini must be charged with notice of this right of the government, it argued, and the work-stoppage provisions were to be "read into" the subcontracts.

The trial court sustained this position and admitted the prime contract into evidence over Guerini's objections. On appeal to this Court, this ruling was unanimously reversed. The subcontractor was not bound by the provisions of the prime contract, this Court held, even though it might have had notice of those provisions, and reference in the subcontract to the plans and specifications for the building was not a valid basis for incorporating the terms of the prime contract itself into the subcontract.[37]

The reference in the subcontract here involved to "contract documents" (R. 8, 9, 11) is exactly the kind of reference to plans and specifications which this Court held in *Guerini* to be insufficient to incorporate the terms of the prime contract itself into the subcontract.

The obvious conflict of the decisions below with *Guerini*, and the failure to administer properly the rule of construction pronounced in *Guerini* justifies the exercise of this Court's power of supervision over the lower federal courts and the grant of certiorari to correct the misapplication of the governing legal rule.

CONCLUSION

For all of the reasons stated, this Court should grant certiorari, summarily reverse the decision of the court below, and remand the case for determination under appropriate state law. The decision below is a serious departure from the constitutional rule allocating responsibility be-

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37. 240 U.S. at 277. *Accord, Woodruff* v. *Hough*, 91 U.S. 596 (1875); *R. P. Farnsworth & Co.* v. *Tri-State Constr. Co.*, 271 F.2d 728 (5th Cir. 1959) (Capehart project); *Battista* v. *Horton, Meyers & Raymond*, 128 F.2d 29 (D.C. Cir. 1942); *H. P. Cummings Constr. Co.* v. *Marbleaid Co.*, 51 F.2d 906 (3rd Cir. 1934); *Miller* v. *Hamilton*, 216 Fed. 131 (8th Cir. 1914); *Shanks* v. *Wilson*, 86 F. Supp. 789 (S.D. W. Va. 1949); *Moses* v. *Edward H. Ellis, Inc.*, 4 N.J. 315, 72 A.2d 856 (1950).

tween the federal and state courts and as such clearly conflicts with and fails to obey *Erie R.R. Co.* v. *Tompkins* and the Rules of Decision Act, 28 U.S.C.A. § 1652. The decision below adopts a theory of decision respecting the scope of an undefined "federal interest" which this Court rejected as recently as January, 1966, in *United States* v. *Yazell.* Considering further the conflict of the decision below with decisions of other courts of appeals, as well as the general importance of the questions raised by this petition for the administration of federal construction and procurement programs, the decision of the court of appeals in the instant case should be reviewed and reversed.

Summary reversal is called for in this case. Such reversal here is consistent with the Court's practice in cases not only where the law is settled by prior decision,[38] but also where the action of the lower court was clearly improper.[39]

Respectfully submitted,

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March, 1966

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38. *Alleghany Ct.* v. *Breswick & Co.*, 355 U.S. 415 (1958); *U. S.* v. *Palletz*, 330 U.S. 812 (1947), and five subsequent cases summarily reversed on the authority thereof reported in 330 U.S. 812 and 331 U.S. 791.

39. *Franklin* v. *Jones Aircraft Corp.*, 346 U.S. 868 (1953); *White* v. *Howard*, 347 U.S. 910 (1954), and *Riss & Co.* v. *U. S.*, 342 U.S. 937 (1952).

APPENDIX A

STATUTORY PROVISIONS

1. The pertinent provisions of the Judicial Code, 28 U.S.C. §§ 1352 and 1652 provide as follows:

§ 1352.

> The district court shall have original jurisdiction, concurrent with State courts, of any action on a bond executed under any law of the United States.

§ 1652.

> The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply.

2. The pertinent provision of the Capehart Act, 42 U.S.C. § 1594 provides as follows:

§ 1594 *Contracts for construction Contract provisions; competitive bids*

(a) The Secretary of Defense or his designee is authorized to enter into contracts with any eligible bidder to provide for the construction of urgently needed housing on lands owned or leased by the United States and situated on or near a military reservation or installation for the purpose of providing suitable living accommodations for military personnel of the armed services assigned to duty at the military installation at or in the area where the housing is situated. Any such contract shall provide that each housing unit in the project shall be placed under the control of the Secretary of Defense, or his designee, as soon as the unit is available for occupancy as determined

by the Commissioner. Any such contract shall also provide that, except for stock held by the Commissioner, the capital stock of the mortgagor (where the mortgagor is a corporation) be transferred to the Secretary of Defense, or his designee, when the housing has been completed as determined by the Commissioner. Any such contract shall contain such terms and conditions as the Secretary may determine to be necessary to protect the interests of the United States. Any such contract shall provide for the furnishing by the contractor of a performance bond and a payment bond with a surety or sureties satisfactory to the Secretary of Defense, or his designee, and the furnishing of such bonds shall be deemed a sufficient compliance with the provisions of section 270a of Title 40, and no additional bonds shall be required under such section. Before the Secretary shall enter into any contract as authorized by this section for the construction of housing, he shall invite the submission of competitive bids after advertising in the manner prescribed in section 152 of Title 41.

3. The pertinent provisions of the Miller Act, 40 U.S.C. §§ 270a and 270b provide as follows:

§ 270a *Bonds of contractors for public buildings or works; waiver of bonds covering contract performed in foreign country.*

(a) Before any contract, exceeding $2,000 in amount, for the construction, alteration, or repair of any public building or public work of the United States is awarded to any person, such person shall furnish to the United States the following bonds, which shall become binding upon the award of the contract to such person, who is hereinafter designated as "contractor":

(1) A performance bond with a surety or sureties satisfactory to the officer awarding such contract, and

in such amount as he shall deem adequate, for the protection of the United States.

(2) A payment bond with a surety or sureties satisfactory to such officer for the protection of all persons supplying labor and material in the prosecution of the work provided for in said contract for the use of each such person. Whenever the total amount payable by the terms of the contract shall be not more than $1,000,000 the said payment bond shall be in a sum of one-half the total amount payable by the terms of the contract. Whenever the total amount payable by the terms of the contract shall be more than $1,000,000 and not more than $5,000,000, the said payment bond shall be in a sum of 40 per centum of the total amount payable by the terms of the contract. Whenever the total amount payable by the terms of the contract shall be more than $5,000,000 the said payment bond shall be in the sum of $2,500,000.

(b) The contracting officer in respect of any contract is authorized to waive the requirement of a performance bond and payment bond for so much of the work under such contract as is to be performed in a foreign country if he finds that it is impracticable for the contractor to furnish such bonds.

(c) Nothing in this section shall be construed to limit the authority of any contracting officer to require a performance bond or other security in addition to those, or in cases other than the cases specified in subsection (a) of this section.

§ 270b *Same; rights of persons furnishing labor or material.*

(a) Every person who has furnished labor or material in the prosecution of the work provided for in such contract, in respect of which a payment bond is furnished under section 270a of this title and who has not been paid

in full therefor before the expiration of a period of ninety days after the day on which the last of the labor was done or performed by him or material was furnished or supplied by him for which such claim is made, shall have the right to sue on such payment bond for the amount, or the balance thereof, unpaid at the time of institution of such suit and to prosecute said action to final execution and judgment for the sum or sums justly due him; Provided, however, That any person having direct contractual relationship with a subcontractor but no contractual relationship express or implied with the contractor furnishing said payment bond shall have a right of action upon the said payment bond upon giving written notice to said contractor within ninety days from the date on which such person did or performed the last of the labor or furnished or supplied the last of the material for which such claim is made, stating with substantial accuracy the amount claimed and the name of the party to whom the material was furnished or supplied or for whom the labor was done or performed. Such notice shall be served by mailing the same by registered mail, postage prepaid, in an envelop addressed to the contractor at any place he maintains an office or conducts his business, or his residence, or in any manner in which the United States marshal of the district in which the public improvement is situated is authorized by law to serve summons.

(b) Every suit instituted under this section shall be brought in the name of the United States for the use of the person suing, in the United States District Court for any district in which the contract was to be performed and executed and not elsewhere, irrespective of the amount in controversy in such suit, but no such suit shall be commenced after the expiration of one year after the date of final settlement of such contract. The United States shall not be liable for the payment of any costs or expenses of any such suit.

APPENDIX B

OPINION OF THE COURT OF APPEALS

United States Court of Appeals for the Eighth Circuit

No. 18,013

National Union Fire Insurance Company of Pittsburgh, Pennsylvania,

Appellant,

v.

D & L Construction Co., et al.,

Appellees.

No. 18,014

D & L Construction Co., et al.,

Appellants,

v.

National Union Fire Insurance Company of Pittsburgh, Pennsylvania,

Appellee.

Appeals from the United States District Court for the Western District of Missouri.

[November 18, 1965.]

Before VOGEL, Chief Judge, and VAN OOSTERHOUT and MEHAFFY, Circuit Judges.

VAN OOSTERHOUT, Circuit Judge.

National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National) appeals from a judgment entered in favor of D & L Construction Company and Associates (D & L) for $711,528.55, such judgment being for

the principal amount of bonds issued by National on behalf of Mojave Electric Company (Mojave) and determined by the court to be in the amount of $530,000 plus attorneys' fees and interest. D & L is the prime contractor on a contract awarded it under the Capehart Act, 42 U.S.C.A. § 1594 et seq., for the building of 700 residential units at Fort Leonard Wood, Missouri. Mojave had two subcontracts on the project; one for $200,000 for the exterior electrical work and another for $330,000 for interior electrical work. National was the compensated surety on the payment and performance bonds demanded by and furnished to D & L, the prime contractor, on behalf of Mojave. National executed and delivered to D & L four bonds totalling $1,060,000, to-wit, (1) a performance bond on the $330,000 interior contract; (2) a payment bond on the $330,000 interior contract; (3) a performance bond of $200,000 on the exterior contract; and (4) a payment bond of $200,000 on the exterior contract.

By cross-appeal, D & L raises the issue that the court erred in denying it full coverage on the four bonds just described and in limiting the aggregate bond coverage to $530,000—$330,000 on the interior and $200,000 on the exterior.

Mojave defaulted on its subcontract. National, when given timely notice of the default, refused to complete the work which Mojave had contracted to do. D & L completed the subcontract work and claims as damages on the bonds the completion costs plus attorneys' fees and interest.

The facts, many of which are stipulated, are set out in the trial court's opinions reported Triangle Electric Supply Co. v. Mojave Electric Co., D.C., at 234 F. Supp. 293 and 238 F.Supp. 815. Detailed findings of fact and conclusions

of law are there set out as well as a discussion of the court's view of the applicable law. We shall not attempt to set forth the rather lengthy and involved factual history in detail here, but will discuss the facts necessary in the course of the opinion.

I. CHOICE OF LAW

[1, 2] Before turning to the substantive legal issues, this court must determine the body of law which governs this appeal. Both agreements between D & L and Mojave specifically stated, "This contract shall be interpreted pursuant to the laws of the State of California." National argues that such specific intent in the subcontracts must be read into the bonds referring to the subcontracts and that California law should control. We disagree. Parties' specific intention concerning what law will control their agreements is binding on courts only where there is a logical basis for applying such law. See 17 C.J.S. Contracts §§ 12(3), 12(4); Weintraub, Contracts and Conflicts of Laws, 46 Iowa L.Rev. 713. National is a Pennsylvania corporation, not a California corporation. The bonding agreement with National was negotiated in the state of Louisiana. The bonds were executed on behalf of National by a Missouri agent. The performance and payment bonded was to be carried out entirely in the state of Missouri. The bond makes no specific provision as to controlling law. Such circumstances show the lack of a logical basis for recourse to California law in this case.

More significantly, this controversy grows out of events in the performance of a Government contract, the prime Capehart contract between D & L and the United States. This court has outlined at some length the federal interest inherent in Capehart projects. Continental Cas.

Co. v. Allsop Lumber Co., 8 Cir., 336 F.2d 445, 449-452. See United States for Use and Benefit of Fine v. Travelers Indem. Co., W.D.Mo., 215 F.Supp. 455, 466-474. In such cases, this court has specifically held with respect to Capehart cases that "the rules of decision that will be applied to the factual situations involved in the various cases will be the rules of decision developed under the Heard and Miller Act decisions." D & L Constr. Co. v. Triangle Elec. Supply Co., 8 Cir., 332 F.2d 1009, 1012.

The Capehart Act requires payment and performance bonds of the prime contractor. There is no specific requirement that the subcontractor furnish bonds. In American Cas. Co. of Reading, Pa. v. Brezina Constr. Co., 8 Cir., 295 F.2d 603, the surety on a Miller Act subcontractor's bond was held to the same rules of construction and contractual liability as the surety for the prime contractor by this court. The instant situation is directly analogous. The trial court properly determined that the controlling law is the federal law developed under the Capehart, Heard and Miller Acts.

II. D & L CROSS-APPEAL.

Consideration will first be given to D & L's cross-appeal as the determination of the issue there presented with respect to the amount of bond coverage has a direct bearing on some of the issues presented by National's appeal.

D & L contends that National is legally obligated on the two performance bonds and on the two payment bonds heretofore described, aggregating $1,060,000 coverage, and that the court erred in determining that National's bonds coverage was limited to $530,000, the amount of the subcontract.

We have difficulty in determining the precise legal basis upon which the trial court determined this issue. The terms of the bonds are clear and unambiguous and on their face provide a total coverage of $1,060,000. The trial court, at pp. 302 to 309 of 234 F.Supp., sets out facts bearing upon this issue and at finding 35 on p. 314 states:

> "The separate payment bonds sued upon were issued by National Union as a result of a mistake, which should not be held to increase the limits of liability established by the performance bonds written on each subcontract in the full amount of the subcontract price."

Apparently upon the basis of our decision in Brezina, supra, the court determined that the performance bonds covered payments due material suppliers and laborers and that the payment bonds here issued were surplusage and issued by mistake. We adhere to our holding in Brezina. We there held that under the circumstances of that case the performance bond covers material claims for which the prime contractor was legally responsible. Conflicting cases are discussed. Our holding is limited to the facts there presented and such case does not go to the extent of holding that a performance bond will under all circumstances cover all of the liabilities contemplated by a payment bond. The case does not deal with the issue of the validity and effect of a validly issued payment bond.

The subcontract pursuant to which the bonds here involved were issued provided for "a performance and payment bond" for not less than 100% of the subcontract price. Clearly the parties had a right to contract for a specific performance and payment coverage.

National in its brief does not attempt to uphold the theory upon which the trial court resolved this issue. In its brief, it states:

"The case evidenced by the record is a clear and simple instance of mutual mistake as to the legal effect of the instruments in question.

* * * * * *

"Doubtless a lawyer under these circumstances would have realized that the legal effect of thus issuing four bonds rather than two would be to afford coverage in double the amount requested.

* * * * * *

"Double the contemplated protection resulted from a mistake as to the legal effect of the use of separate payment and performance bonds—a mistake of law which, while it might seem 'incredible', is nonetheless clearly shown by the evidence to have occurred. If we are to be charitable to D & L and Mojave, the mistake should be classed as 'mutual.' A less charitable interpretation of the evidence, probably undeserved, would convict both Mojave and D & L of having, with full awareness of National's unintended largess, accepted their windfall without a murmur. In either case, the trial court's reformation of the bonds to accord with all of the parties' true intentions was the only result consistent with law, equity, and good conscience."

In response to a question from the court in oral argument, counsel for National conceded that the bonds as written were unambiguous and created liability and that reformation was essential to entitle National to relief. The trial court did not expressly find National was entitled to reformation. However, since reformation if available would support the trial court's decision on the issue raised by the cross-appeal, we shall determine whether National has established a right to reformation.

There is no evidence to support a finding of mutual mistake. If any mistake was made by National, the mistake was one of law. The bonds were contracted for and

executed by an authorized New Orleans agency of National under power of attorney pursuant to a general line of credit of $2,000,000 previously extended Mojave. No combination payment and performance bond forms were available, so the agents chose to execute and deliver separate payment and performance bonds covering each subcontract, and such bonds were delivered to D & L. D & L had nothing to do with the preparation of the bonds or the choice of forms used. The New Orleans office handled the transaction. There is no testimony on the part of anyone connected with that agency to the effect that any mistake, either of law or fact, was made. Enders, a company underwriter at the home office who had nothing to do with executing the bonds, while testifying as a witness insisted the company had made no mistake in delivering the four bonds. Included in his testimony is the following: "You really did intend to sign four bonds then, is that your testimony? A. I said—yes, sir. Q. Oh, I see—A. I didn't—at no time did I say we didn't intend to sign four bonds." Mr. Enders did testify that the company in signing the bonds did not intend an exposure in excess of the subcontract price. Thus, all there is in evidence on mistake is the testimony of an underwriter who had nothing to do with the issuance of the bonds, that the company did not intend to give double coverage. At most, the evidence establishes a unilateral mistake of law on the part of National.

[3] Courts have been wary of granting reformation for a mistake of law without more. Here this court finds no more than a plain mistake of law concerning the effect of a written instrument by a party in the business of executing such instruments. Reformation cannot be granted in such circumstances. 76 C.J.S. Reformation of Instruments § 27; 17 C.J.S. Contracts § 145; 45 Am. Jur. Reformation § 50; 11 Appleman Insurance § 6809.

[4] In order to establish a right to reformation, the burden is upon the party claiming relief to establish mutual mistake by clear, satisfactory and convincing evidence. C. S. Foreman Co. v. Great Lakes Pipe Line Co., 8 Cir., 274 F.2d 61, 65; 76 C.J.S. Reformation of Instruments § 82(b).

[5] Reformation may be granted when mistake exists on one side and fraud or inequitable conduct on the other. 76 C.J.S. Reformation of Instruments § 29. There is absolutely no evidence here of fraud or inequitable conduct on the part of D & L. If National voluntarily chose to fulfill its contractual obligation by furnishing separate performance and payment bonds rather than combination bonds, D & L was under no legal duty to object to such method.

[6-8] Reformation is a remedy not easily won. Equity makes no favorite of a corporate surety. Contracts are construed most strictly against a compensated surety and in favor of indemnity. Home Indem. Co. v. F. H. Donovan Painting Co., 8 Cir., 325 F.2d 870, 874; American Cas. Co. v. Brezina, supra.

While such point is not here reached, we observe that relief if otherwise available might well be barred by National's negligence. See 76 C.J.S. Reformation of Instruments § 46. National should be held to be competent to apprehend the legal effect of bonds it is engaged in the business of writing and selling.

National has failed to meet the burden imposed upon it to establish its right to reformation of the bonds it issued. The bonds by their clear and unambiguous terms provide a coverage for performance in the amount of $530,000 and a coverage for payment in like amount.

The judgment is reversed upon D & L's cross-appeal.

III. NATIONAL'S APPEAL.

National upon its appeal raises the following issues:

A. The court erred in failing to discharge National from all liability under its bonds.

B. The court erred in the assessment of damages against National in various respects.

Such issues will be considered in the order stated.

A.

[9] National urges that D & L made payments on the Mojave subcontract which materially varied from the payment provisions of the subcontract. This issue is discussed in detail by the trial court at pp. 310 to 315 of 234 F.Supp. The court makes findings of fact which we find to be supported by substantial evidence, and upon the basis thereof determines that the provisions of the Miller and Capehart Acts should be read into the performance and payment bonds and that the prime contract is a part of the subcontract, and that when the subcontracts are so construed, the challenged payments made for materials inventoried but not actually incorporated in the work on the construction site were not in violation of the subcontract provisions and that D & L had no duty to the surety to insist upon receipts showing payment for the inventoried materials. Additionally, the court made a finding on conflicting evidence that National before executing the bonds had knowledge that such payments on inventory were customarily made on such projects and were in fact being made on this particular project, and that National had consented to such payments. We are in full agreement with the trial court's treatment on this issue in its well-considered opinion and affirm its determination that National has not established that it is entitled

to a discharge from its bond obligations in whole or in part on the ground of material departure upon the basis of the trial court's opinion.

B.

National raises a number of troublesome problems under its assertion that the court erred in the assessment of damages. The trial court's treatment of the damage issues is covered by pp. 315-317 of 234 F.Supp. and by 238 F. Supp. 815. The principal errors urged will now be considered.

1. National asserts "that portion of the original subcontract price which was not paid by D & L to Mojave should have been credited against the completion costs claimed by D & L." The total agreed amount to be paid Mojave for the performance of its two subcontracts is $530,000. $143,621 of this amount has been paid Mojave, leaving a balance due on the subcontract of $386,379.

We agree with the trial court's view, supported by the authorities it cites, that the bonds here are not penal. They are designed to indemnify the prime contractor for any loss occasioned by failure of the subcontractor to fulfill his contractual obligation. The bonds contain no provision for the payment of a penalty or liquidated damage.

It is undisputed that Mojave defaulted on its subcontract and that timely notice of such default was given the surety, whereupon the surety refused to exercise its right to step in and complete the work. We do not in any way question D & L's right to complete the work and charge the cost thereof to Mojave and its surety. Much of the evidence with respect to completion costs is stipulated and there is no apparent basis for finding that the costs incurred in completing the work were not reasonable and necessary.

There is language in the subcontract which standing in isolation tends to support D & L's view that it can recover all costs incurred in completing the work. However, when the pertinent documents establishing the rights and liabilities of the parties are considered as a whole, it seems clear that the contract limits damage for nonperformance to the loss actually sustained by the default. Paragraph 16 of the subcontract dealing with the consequences of the subcontractor's defaults provides in part:

> "If the unpaid balance of the contract price shall exceed the expense of finishing the work including but not limited to expense for additional managerial and administrative services Contractor shall pay to Subcontractor the amount by which said unpaid balance exceeds such expense; if, however, such expense exceeds said unpaid balance, Subcontractor shall promptly pay to Contractor the amount by which such expense exceeds unpaid balance."

Neither D & L nor the trial court has cited any authority supporting the view that the unpaid balance due on the subcontract should not be credited against the cost of completion. In a similar situation, the computation of damages approved by the Ninth Circuit in Dale Benz, Inc., Contractors v. American Cas. Co., 9 Cir., 303 F.2d 80, 86, clearly shows the unpaid portion of the subcontract price was deducted from completion costs.

72 C.J.S. Principal and Surety § 112 reads, "Where the obligee completes the work himself or has it completed by another, he may recover the amount actually and reasonably expended in completing the contract, in excess of the original contract price." To like effect, see 13 Am. Jur.2d, Building, etc. Contracts § 78 and cases cited in footnote 17 thereto.

[10] The surety's rights and liabilities, absent a specific contrary agreement, are measured by those of its principal. D & L Constr. Co. v. Triangle Elec. Supply Co., 8 Cir., 332 F.2d 1009, 1013; 72 C.J.S. Principal and Surety § 92.

[11] D & L was entitled to have the work subcontracted properly completed for $530,000. Here $386,379 of the agreed compensation for the work Mojave had agreed to do was never paid by reason of Mojave's default. If D & L recovers the full amount of its cost of completion of the subcontracted work, it would realize a windfall profit of $386,379. This is because it would get the $530,000 of subcontracted work completed at a net cost of the $143,621 which it had paid to Mojave. We find no basis in the bond or the contract documents allowing such a windfall. D & L is entitled to compensation by way of damages to put it in the position it would have occupied if the subcontractor had faithfully fulfilled its contract but such is the limit of its rights.

The parties apparently agreed that the completion costs exceeded the $530,000 bond coverage awarded by the court. Such coverage was limited by the court's determination which we have rejected in Division II hereof. Upon remand, the court shall determine the full amount of allowable completion costs and deduct therefrom the unpaid amount of the subcontract price and allow the difference to the extent that such net figure falls within the bond coverage provided.

[12] 2. National urges attorneys' fees should not be allowed to the extent that they are beyond the bond limits. The trial court awarded D & L $25,000 attorneys' fees. The court determined that the subcontract expressly provided for the allowance of attorneys' fees in the present

situation and that hence attorneys' fees are recoverable on the bond under our holding in Triangle, supra. We agree. National does not dispute the foregoing nor does it attack the amount of fees allowed. National does urge that such fees are subject to bond limits and cannot be allowed here as other damages awarded exceed bond limits. Hartford Fire Ins. Co. v. Casey, 196 Mo. App. 291, 191 S.W. 1072, 1076, and other cases cited so hold. D & L concedes such is the law but urges that if coverage within bond limits is available, such fees should be allowed. By reason of other determinations made in this opinion, it appears likely that the attorneys' fees will fall within the limits of the bonds. The judgment entered allowing attorneys' fees is affirmed to the extent that the amount allowed does not exceed the bond coverage.

[13] 3. National raises the issue that pre-judgment interest is now allowable and further urges that in any event such interest has been erroneously computed. The trial court discusses the pre-judgment interest issue at pp. 817-820 of 238 F.Supp. We agree with the trial court's view that the relevant documents contain no express provision for payment of interest and that hence it is necessary to look to state law to measure the subcontractor's obligation to pay such interest. We so held in Triangle. We also are in accord with the trial court's holding supported by the cases it cites that recovery for damages for breach of contract may include damage for delay in payment and that pre-judgment interest may be allowed beyond the bond coverage limits.

[14] National's contention that prejudgment interest was improperly computed must be upheld. Finding 14 indicates that the court computed interest on $530,000 at the rate of 6% per annum from April 4, 1960. Such was the date of D & L's letter to the bonding company

notifying it of Mojave's default and demanding performance. We agree with National that this was a demand for performance, not a demand for money. No specific amount was demanded and no basis for computing damages existed on April 4, 1960. We are aware that the trial court makes a finding that the parties on April 4, 1960, could have reasonably determined the completion cost would exceed the bond coverage. We find no substantial evidence to support such a finding. The letter was written before the attempted subcontracts calling for some $20,000 in excess of Mojave's subcontracts. Apparently no consideration is given to the credit required for the unexpended portion of the subcontract price. Moreover, neither the brief nor the record before us satisfactorily shows when in fact D & L paid the various items of completion cost but obviously most of these payments could not have been made until considerably after the April 1960 default by Mojave.

[15] The pretrial order shows that D & L claims 6% interest on all allowable items of damage under the subcontracts, "said interest to accrue on each such item of damages from date of payment or from the date completion costs [exterior and interior] subcontract first exceeded the contract price—whichever is later." At the trial, the parties stipulated:

> "Let the record show that counsel for D & L & Associates and counsel for National Union Fire Insurance stipulate and agree that interest calculated at the rate of six percent per annum, on the sum shown in the pre-trial order as the completion costs, would accrue from the date upon which the completion costs exceeded the contract amount until April 15, 1964; * * *"

The stipulation then goes on to set out agreed computations made on the foregoing basis. The amount allowed

as interest exceeds the stipulated amounts. National in argument cites the stipulation. No explanation appears in D & L's brief on the court's opinion as to why the stipulation should not be adhered to. Parties are bound by stipulation of facts made unless such stipulations are properly withdrawn or set aside.

[16] No contract provision for payment of interest has been called to our attention. Consequently, to the extent that the stipulation made is not binding, interest should be determined upon the basis of Missouri law. D & L Constr. Co. v. Triangle, supra; L & E Co. v. United States, 9 Cir., (Oct. 8, 1965) 351 F.2d 880.

The judgment entered for interest is set aside. Upon remand, interest shall be computed in a manner consistent with the views here expressed.

4. National contends that the court erred in not subtracting from the final judgment $43,359.10 which National paid toward the settlement of a General Electric claim for materials furnished under a stipulation that the rights of the parties hereto would remain the same as if the G.E. claim remained pending. D & L has not responded to this point. We are unable to ascertain from the record the precise items that are included in the judgment. If National was in fact charged in the judgment computation with the full amount of the G.E. claim, to the settlement of which it contributed, it would of course be entitled to credit for the amount it had previously paid upon such claim. If on the other hand National was not charged with the portion of the G.E. claim which it had previously paid, then the only relief National would be entitled to would be a reduction of its bond coverage to the extent of the payment previously made. Upon this issue, the case is remanded for further consideration and more specific finding.

[17] 5. Finally National urges that completion costs recoverable should be limited to the amounts by which the subcontracted work was relet to Carter and Modern exceeded the $530,000 called for by Mojave's subcontract. Such difference was slighly over $20,000. We agree with the trial court's rejection of such contention. While D & L did obtain new subcontracts, it was unable in the emergency to find responsible subcontractors who could give performance and payment bonds. The new subcontractors in turn defaulted. As pointed out by the trial court, all this difficulty arose out of Mojave's default and National's refusal to take over. We affirm the trial court's holding on this point.

IV.

Because of the trial court's determination of certain issues before it, some issues raised, such as recovery for managerial and administrative expense, allocation of costs between the four bonds, the standing of D & L to sue on the payment bonds, and other issues that may have been material to the disposition of this case, were not disposed of. This opinion should be controlling on the trial court as to issues which we have expressly decided. We do not have a complete record before us and hence are not in a position to make a final disposition of this case. Moreover, it would appear that findings of the trial court on certain factual issues are required.

D & L asks for allowance of additional attorneys' fees in this appeal. The amount to be allowed is referred to the trial court for determination upon remand as well as the issue of the amount, if any, to be allowed for further legal services in the trial court.

Upon remand, a large discretion must be left with the trial court on the question of the extent, if any, that fur-

ther evidence should be permitted or required with respect to unsolved issues remaining in this case.

On D & L's cross-appeal, the judgment is reversed. On National's appeal, we affirm the determination of the trial court that National has not been discharged from its bond obligations in toto or pro tanto.

We also affirm the court's rejection of National's contention discussed in III-B-5 of this opinion and on the allowance of attorneys' fees in III-B-2 subject to the bond limitation.

By reason of the errors pointed out in the computation of damages and the lack of sufficient findings to support other contentions with respect to damages as hereinabove pointed out, this case is remanded to the trial court for redetermination of the amount of damages due D & L on its performance and payment bonds, consistent with the views expressed in this opinion.

APPENDIX C

JUDGMENT

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

September Term, 1965

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Appellant,

No. 18,013 vs.

D & L CONSTRUCTION COMPANY AND D & L CONSTRUCTION COMPANY AND ASSOCIATES,

and

D & L CONSTRUCTION COMPANY AND D & L CONSTRUCTION COMPANY AND ASSOCIATES,

Appellants,

No. 18,014. vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA.

Appeals from the United States District Court for the Western District of Missouri

These causes came on to be heard on the record from the United States District Court for the Western District of Missouri, and were argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that on the appeal of National Union Fire Insurance Company of Pittsburgh, Pennsylvania (No. 18,013), the determination of the District Court that the National Union Fire Insurance Company has not been

discharged from its bond obligations in toto or pro tanto is hereby, affirmed, as is also the rejection of the said District Court of that Company's contention discussed in III-B-5 of the opinion of this Court filed herein, and on the allowance of attorneys' fees in III-B-2 subject to the bond limitation.

It is further Ordered by this Court that by reason of the errors pointed out in the computation of damages and lack of sufficient findings to support other contentions with respect to damages as indicated in the opinion of this Court filed herein, this case, appeal No. 18,013, is hereby remanded to the said District Court for redetermination of the amount of damages due the D & L Construction Company on its performance and payment bonds, consistent with the views expressed in the opinion of this Court.

And it is further Ordered and Adjudged by this Court that on the issues raised on the cross-appeal of the D & L Construction Company, case No. 18,014, the judgment of the said District Court be, and is hereby, reversed.

And It is further Ordered by this Court that costs in this Court be divided equally between the Parties, and the parties having each paid one-half of the cost of printing the record, no costs are to be taxed in favor of either of the parties on appeal in this Court.

November 18, 1965.

APPENDIX D

(ORDER DENYING PETITION OF NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH FOR REHEARING, ETC.)

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

No. 18013.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Appellant

vs.

D & L CONSTRUCTION COMPANY, et al.

No. 18014.

D & L CONSTRUCTION COMPANY, et al.,

Appellants,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA.

Appeals from the United States District Court for the Western District of Missouri

Petition of National Union Fire Insurance Company of Pittsburgh, Pennsylvania, for Rehearing and Motion for Transfer to, and Reconsideration by, the Court en banc, in these causes having been considered, it is now here Ordered by this Court that the same be, and it is hereby, denied.

December 27, 1965.

APPENDIX E

OPINION OF THE DISTRICT COURT

United States District Court for the
Western District of Missouri
Western Division

TRIANGLE ELECTRIC SUPPLY CO., INC.,
Plaintiff,

v.

MOJAVE ELECTRIC CO., et al.,
Defendants.

No. 12904

KOPPERS COMPANY, INC.,
Plaintiff,

v.

CONTINENTAL CASUALTY CO., INC., et al,
Defendants and Third-Party Plaintiffs,

v.

NATIONAL UNION FIRE INSURANCE CO. OF PITTSBURGH, PA.,
Third-Party Defendant.

No. 13232

[Filed October 5, 1964]

MEMORANDUM OPINION, FINDINGS OF FACT, AND CONCLUSIONS OF LAW.

The cross-claim of defendant D & L Construction Company and Associates, the prime contractor on the Fort Leonard Wood Capehart job, against National Union Fire

Insurance Company, the surety on the payment and performance bonds of the defaulted subcontractor, Mojave Electric Company, has been submitted for final decision pursuant to an amended final pre-trial order, the testimony adduced at the hearing, and the parties' stipulation designating the record. That stipulation designates and identifies the various exhibits, pleadings, discovery items, earlier pre-trial orders, depositions, and the transcript of evidence adduced at the hearing held in our Southern Division at Springfield.[1]

Earlier in this case, D & L filed a motion for summary judgment on its cross-claim. Although a great mass of documentary evidence was not questioned by National Union, we refused to rule this case on that motion because of National Union's representation that many of the facts were in dispute.

Subsequent proceedings, however, including the hearing at which two witnesses testified, revealed that the areas of factual dispute are indeed narrow and that the controversies between the parties revolve around questions of law and the inferences that should or should not be drawn from what are, for the most part, the undisputed facts.

FINDINGS OF FACT

In order to place the legal questions in perspective, we make the following findings of fact:[2]

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1. This case has since been transferred to our Western Division at Kansas City. The former Southern Division number is therefore carried in parenthesis. Our action sustaining plaintiff's motion for summary judgment on Count I of this particular Capehart case is reported as Triangle Electric Supply Co. v. Mojave Electric Co., W.D.Mo.1963, 217 F.Supp. 913, affirmed sub nom. D & L Construction Co. v. Triangle Electric Supply Co., 8 Cir. 1964, 332 F.2d 1009.

2. The facts found in the specifically numbered paragraphs to follow immediately are adopted in substance from those proposed by D & L. The modifications in paragraphs 1 through 9 are minor.

1. The original plaintiff, Triangle Electric Supply Company, Inc., is a Texas corporation having its principal place of business in such state. Defendant National Union Fire Insurance Company of Pittsburgh, Penn. (herein sometimes referred to as "National Union"), is a Pennsylvania corporation with its principal place of business in that state. The defendant-crossclaimant D & L Construction Co. and Associates (herein sometimes referred to as simply D & L) is a joint venture composed of D & L Construction Company, a California corporation, and several individuals also residents of California. There is thus complete diversity in the citizenship of the parties. The matter in controversy exceeds $10,000 exclusive of interest and costs.

2. On August 18, 1959, D & L entered into a contract (the "Prime Contract") whereby it undertook, under authority of the legislation commonly referred to as the "Capehart Act" (42 U.S.C. § 1594 ff.), the construction of 700 residential housing units at Fort Leonard Wood, Missouri, for a lump sum price of approximately eleven million dollars.

3. The electrical work required by the prime contract was thereafter subcontracted to Mojave Electric Company by separate written subcontracts, one requiring the performance of all the exterior electrical work for a lump sum price of $200,000.00; a second, the interior electrical work, for a price of $330,000.00.

4. As required by such subcontracts, Mojave, as principal, and National Union, as surety, executed and delivered to D & L the following four bonds:

(a) A "payment bond" relating to the exterior electrical work in a face amount of $200,000.00;

(b) A "payment bond" relating to the interior electrical work in the face amount of $330,000.00;

(c) A "performance bond" relating to the exterior electrical work in the face amount of $200,000.00;

(d) A "performance bond" relating to the interior electrical work in the amount of $330,000.00.

5. The two payment bonds were each conditioned solely upon the prompt payment by Mojave of all labor and material used in the prosecution of the work of the respective subcontracts.

6. Such condition of each of these bonds was at least prior to April 1, 1960, breached by the failure of Mojave to promptly pay for material furnished and labor supplied or performed in the prosecution of the work of the respective subcontracts.

7. The two performance bonds were each conditioned solely upon the faithful performance by Mojave of all of the terms and conditions of the respective subcontracts.

8. By March 28, 1960, Mojave had done nothing toward the performance of either of the subcontracts, other than order, receive and store materials on the job site.

9. On March 28, 1960, D & L notified Mojave and National Union that Mojave was "not maintaining satisfactory progress" as required by the provisions of paragraph four of the subcontracts and that unless satisfactory progress was resumed by March 31, D & L would proceed to avail itself of the remedies provided by said paragraph; i.e., that it would relet the work of the subcontracts and charge the costs of completion to Mojave and National Union. On April 4, 1960, D & L requested National to proceed with the defaulted work in accordance with Paragraph 4(a); but National elected not so to do.

D & L's proposed findings in paragraphs 10 to 22, respectively, relate to the extent of damages. D & L requests

that we find that D & L was damaged $78,219.71, as a result of the breach of the exterior payment bond, and $28,479.41, as a result of the breach of the interior payment bond. In regard to the exterior performance bond, D & L requested a finding that more than the $200,000.00 face amount was spent to complete Mojave's defaulted subcontract, and a finding for reasonable attorney's fees in the amount of $10,000.00, together with interest.

In regard to the interior performance bond, D & L requested a finding that $318,402.00 was spent to complete the defaulted Mojave subcontract, and that interest and a reasonable attorney's fee of $15,000.00 should also be allowed.

The various pre-trial stipulations and pre-trial orders have dealt with the actual dollars involved in particular categories of damage. The proposed findings of the parties in regard to particular amounts show a large area of agreement as to particular amounts but they also show some disagreement in regard to other particular amounts.

National Union has noted of record that its requested finding of fact F-39 was limited "to the amounts potentially involved in various items of damages sought by D & L in the event the Court should hold in its favor" and that "no findings were requested as to the total amount of final judgment. * * * because of the great number of unresolved legal issues bearing on the recovery and amount of various categories of damages."

National Union also suggested in that letter, and we think it a good suggestion, that we should "allow the parties to consult with each other as to the amount of the judgment, if any, after the Court has made its decision on the various issues raised by the requested Findings of Fact and Conclusions of Law."

In our order at the end of this Memorandum Opinion we shall direct further proceedings consistent with that thought. We shall not, therefore, either accept or reject any of the specific requests of the parties that include particular dollar amounts as included, for example, in paragraphs 10 through 22, inclusive, of D & L's requested findings.

In regard to the affirmative defenses asserted by National Union we make the following findings of facts:[3]

23.[4] The execution of the instant bonds by National Union was effected through its New Orleans agents, the firm of Emery and Kaufman, Ltd. Sometime prior to December, 1958, that agency was contacted by one Marshall Brown concerning the possibility of becoming, on behalf of National Union, the bonding agency for the construction activities of Mojave Electric Company.

24. Brown was instructed to obtain the customary financial information. After making the usual investigation, such as obtaining audited financial reports and making independent verifications with architects, prime contractors, etc., L. L. McKinney, who was handling the matter on behalf of the Kaufman agency, reviewed the resulting finan-

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3. We again follow the paragraph numbers contained in D & L's requested findings of fact in regard to these further particular findings of fact. It is to be understood, of course, that still additional findings are made elsewhere in this memorandum opinion and that they supplement those we now find.

4. National Union contends that the findings made in this paragraph and paragraphs 24, 25, 26, and 28 to follow, all relating to National Union's investigation of Mojave's financial resources, the establishment of the line of credit, and the like, are immaterial and irrelevant. As we will note later, we believe the extent of National Union's general and particular investigation of the particular job it was bonding is most material in regard to the affirmative defenses it has pleaded.

cial information with the auditor, Heenan, and on the basis of that information and investigation recommended the establishment of a line of bonding credit by National Union for Mojave.

25. Under a "line of credit" an agent is authorized to execute on behalf of the company any number of bonds to the designated limit, consulting with his home office only when there is a departure from the established line, a bonding procedure distinguished from the alternate practice where the agent must obtain from his principal specific authority to bond a particular project.

26. Mojave's line of credit with the Kaufman agency was established at $1,000,000.00 in December of 1958. In October, 1959, and after obtaining additional information and documentation, including for added protection an indemnity agreement signed by Mojave's principal officer and his wife on April 23, 1959, showing a personal worth exceeding $250,000.00, the authorized line of credit was increased to $2,000,000.00.

27. Although as noted the instant subcontracts were executed on August 18, 1959, execution of the bonds therefor was for unexplained reasons delayed until December 18, 1959, when Heenan sent the following "Speedmemo" to McKinney: "Please execute bonds on attached contracts: 330,000.00 and 200,000.00—Rush! Job progress report now in progress."

28. Although not required, since it was a line of credit client and because they already had a general indemnity agreement, the signature of one Troupe, an employee in Mojave's New Orleans office was obtained on partially filled in application forms. Without further investigation and with no particular investigation of the Fort Leonard Wood

Capehart construction project, two payment bonds and two performance bonds were signed by Kaufman as attorney in fact for National Union and countersigned by McKinney as he was authorized to do under company approved lines of credit. Presumably, in accordance with practice, execution reports were then sent to the home office. The bonds themselves were mailed to Kansas City, Missouri, for countersignature by National's Missouri agent, the Ridge-Spellman Insurance Agency. They were finally delivered by Mojave to the attorney for D & L on January 13, 1960.

29. Under the financing arrangements peculiar to a Capehart project, the prime contractor is required to form one or more Delaware corporations which serve as a conduit for funds from the private lender to the prime contractor during the construction period. In accordance with the terms of the building loan agreement advances are made to the prime contractor on a monthly basis. According to the categories established in the "trade payment breakdown", periodic progress is measured as a percentage of the lump sum contract price, rather than the usual quantities of completed work, and the monthly payment is the single dollar amount equivalent to that percentage. The monthly percentages are established by informal negotiation between the prime contractor and the government inspectors, here the designated representative of the Corps of Engineers, and are measured as the total of physical completion plus the agreed value of acceptable materials delivered to and suitably stored on the job site but not incorporated into the buildings composing the project. Since the materials have thus been paid for in the inventory stage, their value is later deducted from the sums which

would otherwise be due as physical completion in later progress payments.[5]

30. In subcontracts where material represents a major portion of the total subcontract price, purchases of material must as a practical matter be financed by periodic payments for material inventories as well as physical completion. The materials are ordered from the supplier in total quantities, delivered to the job site and stored in a designated area adjacent to the construction site (an area which has a short term lease on it which is also given as security for the mortgage in addition to the construction site). Once the materials are stored on this area, the storage area, the subcontractor supplying the material furnishes the prime contractor his estimate of the value of the materials so stored. The prime contractor informally turns this over to the military inspector who makes a physical examination of the inventory and advises the prime contractor of the value which he will approve as to each subcontractor. The prime contractor, in turn, advises the subcontractor of the amount of money which will be approved as an inventory allowance. The subcontractor then submits a formal requisition or billing in the approved amount which the prime contractor includes with those of other subcontractors in its monthly application to the lender for funds. When the

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5. National Union objects to the relevancy of the economic facts concerning the established Capehart payment procedures. Our determination that those procedures, required and made necessary as they are by statute, must be read into the bonds, along with the prime contract and that statute, (as we shall develop in some detail later) affords one base for our adverse ruling in regard to National Union's objections to this paragraph and to similar objections made in regard to paragraphs 29, 30, 31, 33, 35, 38, 41, and 55 to follow.

We also add that we believe that additional support for this and the other findings mentioned will be found in the contract documents and other documentary evidence stipulated in this case, as well as in the deposition testimony to which our attention was directed by the respective parties.

prime contractor receives the requested funds from the lender through the Delaware corporation, he in turn pays the subcontractors the portion thereof representing the requisition of the particular subcontractor.

31. Each of the Mojave subcontracts was executed on a printed form of subcontracting agreement which D & L's counsel adopted from that used on an earlier Capehart project (where Mojave had also been the electrical subcontractor and National Union its surety) and used on this and several other Capehart projects involving over 200 subcontractors, all paid in the above manner.

32. Each form of subcontract provided as to the manner in which progress payments would be made to a subcontractor:

> "3. For the strict (but not substantial) performance of all its obligations hereunder, Contractor shall pay to the Subcontractor the following amounts and in the following manner: The total amount of $ (lump sum price inserted) payable at the rate of 90% of all material and labor in place as shown on the following schedule:
>
> (payment to be based upon actual progress)
>
> and payment will be made monthly as Contractor receives funds from the lender for same, and the balance of 10% on the completion of the prime contract for each mortgage area and when the contractor has received final payment from the lender for the work performed by Subcontractor.
>
> * * * * * *
>
> "9. Subcontractor shall submit to the Contractor an application for each payment, and releases, receipts or other vouchers evidencing payment for materials and labor together with such additional evidence bear-

ing on the right to the payment claimed as Contractor may direct."

33. The above clauses were included in subcontracts on the other Capehart projects where this same form was used, including those at White Sands, New Mexico, and Yuma, Arizona, where Mojave was also the electrical subcontractor and National Union was its surety.[6]

34. As the officer of National Union testified, "[On-site material] is a normal condition or item that a contractor would get paid for, on-site material, materials which are stored on the job site, and presumably for which he is being billed or has paid for. This happens in every contract, whether it is Capehart or anything."

35. Paragraph 9 of the subcontract, using the discretionary word "may", was to permit the prime contractor to require of the subcontractor such receipts in the event they were required of the prime by the government under Article IX of the Housing Contract; otherwise, there

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6. Our modification of D & L's suggested findings reflects our view that our ultimate determination of the meaning of the clauses of the subcontracts must be ascertained and based on more factual data than simply the statement of the draftsman that he intended, by his choice of language, "to provide by the above clauses for the payment of material inventory as well as physical progress," as the D & L finding is suggested.

We determine elsewhere that under all the facts and the applicable law which requires the subcontract and its bond to be read in the light of the prime contract and the statute, that all the parties must be held to have contemplated that material inventory would be paid for when and if approved by the Corps of Engineers as a part and parcel of the usual Capehart financing procedures and that the very purpose of a subcontractor's bond was to insure the prime contractor that it would be protected against the subcontractor's default in regard to material purchases. Those and other similar determinations require that the clauses be construed in D & L's favor. This footnote is to make clear that we consider the expressed intentions of the draftsman as only one circumstance that must be taken into account in our consideration of this case.

was no other evidence bearing on the right to a payment other than copies of invoices, the formal requisition for funds, and the approval of the inspector, unless the prime contractor had been alerted by claims of unpaid materialmen.

36. The date and amount of all payments by D & L to Mojave and the contract with respect to which paid were as follows:

Date	Contract	Amount
11/16/59	Exterior	$50,000.00
12/29/59	Exterior	25,248.00
12/29/59	Interior	68,373.00

37. Each of these payments was made pursuant to signed application of Mojave on the standard form of "Subcontractor Requisition for Funds," accompanied by a formal progress billing and a detailed inventory of materials represented by Mojave as being suitably stored on the job site. No "releases, receipts or other vouchers" evidencing payment by Mojave to the supplier of the materials were presented by Mojave or requested of it by D & L.

38. In order to ascertain that the materials listed in the inventories and for which payment was requested in the above requisitions were acceptable materials and were suitably stored on site so that payment therefor would be forthcoming from the lender, D & L obtained the customary Project Inspection Report from which the responsible official of the Corps of Engineers attested that all of the materials for which payment was being made were stored on the site in an acceptable manner and that the amounts for which payments were made represented acceptable work and materials.

39. By December 29, 1959, D & L had received from the lender the sum of $75,248.00 certified by the Resident

Engineer and approved by the Contracting Officer as the value of uninstalled acceptable materials for use in the exterior electrical subcontract stored in an acceptable manner on the mortgaged property but not incorporated into the work.

40. By December 29, 1959, D & L had received from the lender the sum of $68,373.00, certified by the Resident Engineer and approved by the Contracting Officer, as the value of uninstalled acceptable materials for the electrical work, interior, stored in an acceptable manner on the mortgaged property but not incorporated into the work.

41. The method used by D & L in making the periodic progress payments to its subcontractors on this and other Capehart projects accorded with the intent and understanding of all parties and was consistent with recognized custom and practice. D & L, Mojave and National Union, all recognized that Mojave was, on December 29, 1959, entitled to these payments of $68,373.00 and $75,248.00, subject only to its duty to furnish the bonds called for in the subcontracts.

42. The making of the above payments did not materially alter or affect the nature or extent of the obligations originally assumed by Mojave under the aforesaid subcontracts nor those assumed by National in executing the instant bonds.

43. Each of such payments was made prior to the delivery to the obligee of the bonds in suit, but not before National Union was obligated on the respective bonds.

44. National Union is in the business of writing, for compensation in the form of premiums, payment and performance bonds on construction projects and was indemnified by its principal to the extent of the indemnification agreement of record.

45. National Union's rights might, perhaps, have been prejudiced if the payments to Mojave were represented as physical progress and that progress had not actually been accomplished; or, if for material inventory, the materials had not actually been on site; or the proceeds of the payments had knowingly been applied to jobs other than this, or other than those bonded by National Union.

46. No factual basis for prejudice to National Union has been shown in this case. No physical progress was falsely represented. Mojave's requisitions and inventories, certified by the inspectors, justified D & L in concluding that the material inventories were "on-site." National Union made no investigation as to the subsequent use of these funds by Mojave. National Union adduced no evidence indicating the application of these payments to any project or any use other than the prosecution of the work at Fort Leonard Wood. No evidence of knowledge on the part of any of the parties to such was adduced by anyone.

47. On December 31, 1959, National Union's total exposure on projects on which it had bonded Mojave was in excess of $1,000,000.00.

48. Mojave requested the instant payments in order to finance and pay for the purchase of material and its payroll and overhead costs on the Fort Leonard Wood project.

49. All payments for material inventory are deducted from amounts which would otherwise be later due and if not paid upon initial request are reinventoried and re-requested in subsequent monthly invoices.

50. National Union was not prejudiced by the making of any of the above payments to Mojave.

51. National Union did not adduce any evidence as to the fact, nature, or extent of any prejudice resulting from any one of the above payments.

52. All such payments were made prior to the delivery of the bonds to the obligee, D & L, on January 13, 1960.

53. Prior to the making of the payments of December 29, 1959, National Union's agent, Kaufman, was informed by Mojave as to the amounts in which the payments were being requested and would be made; of the circumstances out of which the demand for payment arose; and, specifically, that they were for material inventories. Kaufman demanded that the payments be made as due under the subcontracts. When D & L refused to make the payments unless the execution of the bonds be confirmed in writing by National Union, Kaufman, for the specific purpose of inducing D & L to make the payments, sent D & L a telegram confirming that the bonds had been executed by him.

54. National Union, under all the facts, must be held to have consented to the making of the payments of December 29, 1959.

55. National Union knew at the time these bonds were executed from the practice and its experience on this and previous Capehart projects that a subcontractor's periodic progress payments would include payment for material inventoried on-site but not actually incorporated into the work.

56. Neither of National Union's agents, Kaufman or McKinney, were acting upon any misrepresentation of fact either when the $2,000,000.00 line of credit was established in October of 1959, or when these particular bonds were executed by them on December 23, 1959. No misrepresentations were contained in the material submitted by Mojave

upon which the line of credit was established and the bonds written. No other representations were made by Mojave.

57. No information was ever obtained from, or representations made by, any representative of the obligee, D & L, particularly not prior to December 23, 1959. Mr. Kaufman indeed denied that there was ever an occasion upon which any representative of D & L could have made a representation or disclosure of any material fact.

58. National Union did not rely upon any information furnished by D & L in establish ng the line of credit or in executing the instant bonds but relied solely upon its usual, independent investigation of Mojave's affairs and the information furnished by Mojave in the course thereof; nor was there any prior occasion upon which D & L could have made disclosure of any material facts.

59. By December 29, 1959, the bonds in question had already been executed by National Union's agents.

We can not accept the language of the suggested findings of either party in regard to exposure of National Union on the four bonds mentioned in the finding made in paragraph 4 above, although, in result, we are in agreement with National Union's conclusion.

On the face of the four bonds, and by adding the amounts there set forth, it would seem that National Union has an exposure of twice the amount of the subcontracts bonded. There is no dispute, however, but that the bond applications called for only two, rather than four, bonds, totaling $530,000.00; that only two bonds of that amount were referred to in the Speedmemo, the telegram, and the letter of transmittal (although they were referred to as "performance bonds" in that letter); that premiums were paid on the basis of a $530,000.00 exposure rather than a $1,060,000.00 ex-

posure; and that D & L's counsel at least once in an earlier stage of this proceeding referred to the total coverage of $530,000.00, rather than the apparent face amount of $1,060,000.00 (page 66 of McKinney deposition).

Our acceptance of what might on its face appear to be an incredible story that an established surety company admittedly executed bonds totaling $1,060,000.00 when it actually intended to be bound only to the extent of $530,000.00 is justified by the revelations in this record as to how National Union elected to obligate itself in connection with this particular Capehart housing project and how surety companies generally operated in regard to Capehart bonds.

By the time Mojave had defaulted and D & L was trying to get a new take-over contractor who could obtain a bond, it was apparent that "owing to developments in the industry of building houses for the Government, it had become almost impossible to bond the subcontractors" (Fitzpatrick deposition, p. 30).

The hearings before the Subcommittee on Military Construction of the Senate Armed Services Committee on September 1, 1960, (86th Cong. 2nd Sess.) in connection with Work Stoppages on Capehart Housing Projects, was centered on projects on which Hal B. Hayes was the prime contractor. Senator Capehart's letter to Commissioner Zimmerman of June 20, 1960 (page 51 of the Hearings), states that he was reminded that the difficulties presented by the Hal B. Hayes projects "closely parallel a situation called to my attention last year."[7]

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7. We recognize, of course, that those hearings are only within our judicial notice. We cite those hearings in this jury-waived case solely for background purposes and to illustrate that what happened on the Fort Leonard Wood project, though highly unusual from a business practice viewpoint, was not factually unique so far as Capehart projects went. The ultimate litigation in connection with one of the Hal B. Hayes Capehart

More pertinent to the facts of this case is the testimony of the individual who was probably most responsible for National Union's writing the bonds. He testified that a Capehart project "was a rough case to write" (page 4 of McKinney deposition); that at the time the bonds were executed he had been familiar with the Capehart program only "in a limited way" and that "in fact, even today my knowledge is somewhat limited as to the full characteristics of a Capehart project" (page 5 of McKinney deposition).

Mr. McKinney did, however, know that the three companies his firm represented, Continental, Seaboard, and National Union, had indicated to him that "the Capehart projects were not the best type of business * * * in the surety mind it was not the type of business to handle" (pages 5-6 of McKinney deposition).[8]

Mr. McKinney testified that he could not testify definitively concerning the reasons why Capehart projects were difficult to finance because "at that time my knowledge was so limited [that] if you were to question me as to how the financing is set up in a Capehart project, I couldn't answer you, because I don't know. I have never been involved with it enough to really know" (page 7 of McKinney deposition).

Mr. McKinney did, however, state to National Union in his recommendation that Mojave's line of bond credit be in-

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projects discussed in the hearings is reported as Continental Casualty Company v. United States, 5th Cir. 1962, 308 F.2d 846. That case dealt in part with the "fourth tier" supplier defenses raised by the surety of a prime contractor mentioned in Senator Capehart's letter and with which we also dealt in our last memorandum opinion in the Fine v. Travelers Indemnity Co., consolidated cases W.D.Mo.1964, 233 F.Supp. 672, Nos. 1852, 1877, 1901, 1937, 1945 and 1954, decided September 8, 1964, but not yet reported.

8. All three companies, incidentally, are present parties litigant in various of the Fort Leonard Wood Capehart cases that pend in this Court.

creased to $2,000,000, that "the problem of collecting from 'Uncle Sam' is tough, especially on negotiated work done by Mojave" (page 3 of McKinney Exh. 6). The Edwards Air Force Base Capehart job was identified in that recommendation as one of the jobs that "the U. S. Government has required that Mojave be subcontractor."[9]

Mr. Kaufman, the head of the firm representing National Union, was also only generally familiar with the financing of a Capehart project (page 96 of Kaufman deposition). His particular familiarity with the status of the particular subcontracts here involved (which had been executed on August 18, 1959) at the time he telegraphed D & L that the bonds had been executed and were in force is revealed by the following testimony:

> "Q. Let me ask you, Mr. Kaufman, if prior to sending the telegram, you made any investigation into the status of the work, if any, done by Mojave at Fort Leonard Wood, Missouri?
>
> "A. I did not.
>
> "Q. Was any such investigation made under your direction or control?
>
> "A. There was not.
>
> "Q. And it is your testimony that you sent such a telegram in reference to such bonds without any inquiry as to the status of the work; is that correct?
>
> "A. That is correct."

Mr. Enders, a bond underwriter and an officer of National Union, testified at the hearing. He testified that he believed his experience with Capehart projects had been

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9. It is of only passing interest to note that Triangle Electric, the plaintiff in this action, was also plaintiff in the Fort Bliss litigation and that the material it supplied in both cases was supplied to Mojave Electric Company. See page 847 of 308 F.2d. Mojave's subcontracts in both cases were bonded by National Union. See pages 49-50 of McKinney deposition.

confined to "one or two Capehart projects other than this one" (Tr. 54). He never talked to Mojave or D & L concerning the bonds here involved (Tr. 51) and knew nothing about the payments (Tr. 53-54) before approving the execution of the bonds.

In regard to how four rather than two bonds were issued, Mr. Enders testified on direct examination as follows:

> "Q. * * * can you tell me why four bonds, two separate bonds on each subcontract, were issued instead of only one on each subcontract? * * *
>
> "A. I might only say this. The contract itself called for one bond, covering performance and payment in an amount equal to a hundred percent of the contract price. * * *
>
> Now, in this particular instance here, and at the time that these bonds were required, to the best of my knowledge, National Union did not have one document in print that covered both performance and payment bonds. Therefore, we did what we considered at the time to be the most expedient thing, and naturally, as in all of these instances, they want the bond immediately, or sooner. So we executed a performance and payment bond, separate performance and separate payment bond, each in an amount equal to the contract price." (Tr. 37-38)

On cross-examination, he testified:

> "Q. * * * Now, did I understand your testimony to be that if you had some other form available you would have written on some other form, is that what you are here saying?
>
> "A. If the company had had in print at that time a joint bond which encompassed both performance and labor and material, we would have executed that form.

"Q. And you didn't have such a form available for this, is that right?

"A. To the best of my knowledge, there was none available then and there is none available today.

"Q. * * * Have you ever seen a form for a subcontractor on a Capehart job?

"A. I can't recall whether I have or not.

"Q. What did you do when you found you didn't have a form?

"A. Well, the most expedient thing was done, apparently." (Tr. 55-56)

And, after counsel had indicated they had completed their examination, we asked the following questions and received the following answers:

"THE COURT: As I understand your testimony, there was no form whatever prepared by your company that would fit the situation covering liability of a subcontractor under a Capehart job? Did you so testify?

"THE WITNESS: Yes. No, there was no form.

"THE COURT: There just wasn't any animal in existence that fitted that?

"THE WITNESS: Could I elaborate on that a bit?

"THE COURT: Yes.

"THE WITNESS: There is no—we have no company form in print, in print, or that we could have used which would cover a performance and payment obligation in the penal sum of this—or the amount of contract in this instance. It may have been possible to draft one manually, but we never do it, and this has been—not only with National Union Insurance Company but a great many other surety companies, have done the same thing here. They have executed two bonds, with the thought in mind that their liability is limited to the one form.

"THE COURT: Well, this is what I want to get to, because you said because of the absence of this form you felt it was—I think you used the word 'expedient'—

"THE WITNESS: That is right, sir.

"THE COURT: —to actually execute four bonds, and you knew you were actually executing the four?

"THE WITNESS: We knew we were executing four bonds.

"THE COURT: And was it your feeling that by executing the four, you were expediently covering the liability under the Capehart subcontract liability?

"THE WITNESS: And in the terms of the contract between the prime and the subcontractor." (Tr. 66-67).

Of course, at this late [stage] in the course of this proceeding,[10] National Union, through Mr. Enders' answers to counsel's leading questions, suggests that it never intended to have more than $530,000.00 exposure. We note the following colloquy:

"Q. (By Mr. Smalley) Mr. Enders, by issuing two bonds on each of these subcontracts, was it the intent and belief of the company that it was doubling its exposure, that it was exposing itself in the amount of twice the contract price?

* * * * * *

"A. It was not the intent of the company to issue two bonds each in the amount—each in an amount equal to the contract price.

"Q. The company believed, or the person issuing the bond, at least, since the company is an artificial entity, believed the exposure to have been $330,000 un-

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10. The whole problem of four versus two bonds, and the extent of National Union's exposure was not injected into this case until shortly before the final hearing. Mr. Enders testified that the problem had been "recalled" to his attention only within the last few weeks before then (Tr. 60).

der one subcontract and $200,000 under the other, is that right?

"A. Correct." (Tr. 44).

We have not outlined the testimony as fully as we have for the purpose of indicating our acceptance of National Union's conclusory testimony that it did not intend a bond exposure in excess of $530,000.00. We have made that outline to illustrate the necessity for utilizing aids of construction other than the after-the-fact testimony of the parties in our determination of the intent that must be legally attributed to them at the time the various contractual relations were established.

The evidence in this case makes clear that no one was paying any real attention to the language contained in any of the printed forms of contract that were executed by the respective parties; that the particular language there used was not the subject of negotiation between the parties here involved that could be said to have led to the choice of particular language patterned to fit this particular project. We think the entire record demonstrates that everyone concerned never gave much real thought to what their respective legal rights might or might not be in the event of default.

Our ultimate finding that the amount of National Union's exposure should be limited to $530,000.00 is based upon a specific application of legal principles that we believe must be applied to several aspects of this case. We turn to a discussion of those principles.[11]

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11. Having completed our review of the findings of fact specifically requested by D & L, we state for purposes of the record that we expressly reject all of National Union's suggested findings of fact although it is quite apparent that many of them are quite consistent with the findings we have accepted at the suggestion of D & L. We have adopted this procedure and make this statement in order that the case may be more conveniently briefed in the appellate court should an appeal be ultimately taken.

CONCLUSIONS OF LAW

[1] In ruling plaintiff's motion for summary judgment on Count I in this case, we took as our point of beginning the legal principle we first announced in United States v. Travelers Indemnity Company, W.D.Mo.1963, 215 F. Supp. 455, namely, that for the reasons stated in detail there (and we again expressly adopt all applicable language here) "the rules of decision that will be applied to the factual situations involved in the various [Capehart Act] cases will be the rules of decision developed under the Heard and Miller Act decisions" (see page 914 of 217 F.Supp.).

Counsel for D & L, appellant in the Court of Appeals, in Triangle Electric, in which we sustained plaintiff's motion for summary judgment (217 F.Supp. 913), contended that we had erred in so ruling. The Court of Appeals, however, held that "[u]pon the record before us, we believe that the trial court properly determined that proposition" (see page 1012 of 332 F.2d).

And in Continental Casualty Company v. Allsop Lumber Co., 8 Cir. 1964, 336 F.2d 445, decided August 26, 1964, (not yet reported), the Court of Appeals discussed in greater detail the rationale of Travelers Indemnity. We have discussed Allsop Lumber in considerable detail in our most recent Capehart memorandum opinion (to which we made reference in footnote 7 above). What we said there need not be repeated here; we again adopt the applicable language for this opinion by this reference.

In general, therefore, it must be said at the outset that our conclusions of law in regard to this branch of this case will rest upon the same base upon which we rested our determination of plaintiff's motion for summary judgment in Triangle Electric and the various other Capehart cases we have recently decided.

We shall also reiterate in some detail and apply another facet of our determination in Travelers Indemnity (noted with approval on page 451 of 336 F.2d of Allsop Lumber's opinion) that "all substantive provisions of the Miller Act and the Capehart Act were to be read into Capehart bonds."

We recognize, of course, that National Union's subcontractor bonds, strictly speaking, can not be described as either Miller Act or Capehart Act bonds. But that does not answer the question of whether cases construing subcontractors bonds on Miller Act construction projects are to be considered as persuasive in cases in which construction must be given to the similar subcontractors' bonds on Capehart projects. It is our conclusion that reason and the considerations to be presently mentioned require that we again follow the general pattern established by the Miller Act cases although we are dealing with a subcontractor's bond instead of a prime contractor's bond. Such has been the rule applied in Miller Act cases and we believe that logic requires like treatment in regard to subcontractor's bonds in Capehart cases.

Both the payment and performance bonds here involved make specific reference to the subcontracts between D & L and Mojave dated August 18, 1959. Both subcontracts on their faces show that each was identified as a part of the Capehart housing to be constructed at Fort Leonard Wood. Both subcontracts specifically incorporated all the "contract documents" of D & L's prime contract into each subcontract.[12] Paragraph 18 of the General Provisions

12. National Union's argument on page 54 of its argument in support of requested conclusions of law 4 that "the reference in Paragraph 4 of the subcontract to the 'Contract Documents' clearly provides no basis for * * * a wholesale incorporation by reference" is untenable. As we shall note later in detail, the subcontracts and the subcontractors' bonds must be read in light of the prime contract and the statute under which the government housing is authorized.

applicable to all Armed Service Housing Projects, attached to and made a part of the prime contract, demonstrates the interrelation between the prime contract and the contemplated subcontracts to be let under it. By that paragraph the prime contractor is required to insert particular paragraphs of the General Provisions of the prime contract into all subcontracts let under it.

Paragraph 31 of the General Provisions, one of the paragraphs specifically required to be inserted into all subcontracts, provides that accrued payments on advances due the eligible bidder may be withheld in amounts considered necessary to pay laborers and mechanics employed by the eligible bidder or any subcontractor. The substance of that paragraph of the prime contract appears as paragraph 51 of the subcontract. That paragraph of the subcontract, incidentally, provides that "payments or advances" to the subcontractor may be withheld, indicating that "advances" as well as "payments" were within the contemplation of the parties. More broadly, that paragraph illustrates the interdependence of the payment procedures of the prime and subcontracts let under it.

[2] All the parties were bound to know the procedures for payments to the prime contractor as detailed in Article IV of the prime contract. All the parties must be held to have known that the prime contractor would be placed in funds to pay for "uninstalled acceptable materials suitably stored on the mortgaged property in a manner acceptable to the Contracting Officer, plus the cost of the portions of the work acceptably completed, as approved by the Contracting Officer, computed in accordance with the amounts assigned to the several items in the Trade Payment Breakdown * * * less 10% and less prior advances."

Although the language is a bit different, Article IV of the Capehart prime contract provides in substance the same familiar payment procedure contained in Article 16 of a regular standard federal construction contract. See U. S. Standard Form No. 23 (41 U.S.C.A.App. § 54.13 at page 306). A comparison of U. S. Standard Form No. 25A (41 U.S.C.A.App. § 54.16), the standard federal payment bond, and U. S. Standard Form No. 25—B, the standard federal performance bond (41 U.S.C.A.App. § 54.17), with the payment and performance bonds written by National Union in this case, reveal a great similarity in substance, although again, there is some slight difference in form of language.

The language in the payment bonds issued by National Union in this case contained an express recognition that Mojave would make prompt payment for materials furnished under the terms of the contract "whether or not the said materials or labor entered into and became component parts of the work or improvement contemplated in said contract." It is therefore apparent that National Union, as the compensated surety, wrote a bond in which it expressly recognized what its witness, Mr. Enders, testified was "a normal condition or item" in any construction contract, namely, "that a contractor would get paid for on-site material, materials which are stored on the job site, and presumably for which he is being billed or has been paid for" (Tr. 54). As Mr. Enders correctly explained, "This happens in every contract, whether it is Capehart or anything" (Tr. 54).[13]

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13. It should be noted, as we now turn to a discussion of comparable Miller Act cases, that National Union also wrote Miller Act bonds and therefore must be held to be acquainted with the standard government payment procedures on such construction projects. We also again note, as we earlier noted in footnote 41 on page 471 of 215 F.Supp., in our memorandum opinion in Travelers Indemnity, that surety companies view the risk on

It is well known that the utilization of bonds on subcontracts increased following the decision of MacEvoy v. United States, 322 U.S. 102, 64 S.Ct. 890, 88 L.Ed. 1163 (1944). On page 110 of that case, the Supreme Court commented on the "practical considerations" that must be taken into account by a court faced with the construction of the language of the Miller Act and of the bonds required thereunder. It was there noted that "[i]t is easy for the prime contractor to secure himself against loss by requiring the subcontractors to give security by bond, or otherwise, for the payment of those who contract directly with the subcontractors."[14]

Judge Matthes' opinion in American Casualty Co. of Reading, Pa. v. Brezina Const. Co., 8 Cir. 1961, 295 F.2d 603, dealt directly with the problems of what rules of construction should be applied to a bond of a subcontractor on a Miller Act project which had been required by the prime contractor. In that case Brezina was the prime contractor, bonded under the Miller Act by General Insurance Company of America.

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construction bonds on government housing built under the Capehart Act as the same sort of risk as is involved on bonds required by the Miller Act on other government construction, and that, accordingly, such companies charge the same premiums on Capehart bonds as they charge on Miller Act bonds.

14. The quoted language is a direct paraphrase of the language of United States, for Use of Hill v. American Surety Co., 200 U.S. 197, 204, 26 S.Ct. 168, 50 L.Ed. 437 (1905), construing the Act of 1894, Mankin v. United States, for Use of Ludowici-Celadon Co., 215 U.S. 533, 540, 30 S.Ct. 174, 54 L.Ed. 315 (1910), construed the Heard Act of 1905, accepted what had been said in Hill, and pointed out still another way a prime contractor could protect himself, i. e., by requiring that payments on the subcontract would be withheld until full releases for material and labor contracted by the subcontractor be furnished by the subcontractor to the prime contractor. Of course, if the subcontractor is required to and does in fact furnish a bond, then the prime contractor lets the surety worry about obtaining the releases because the failure of the subcontractor to pay his suppliers is the exact condition of the bond. Such has been the law and the practice in the construction industry for over a half century.

Brezina subcontracted the plumbing and heating portion of the prime contract to A & A Contractors, Inc. As was true in this case, Brezina, the prime contractor in the cited case, provided in its subcontract that its subcontractor, A & A, would furnish a bond in the full amount of the subcontract. American Casualty Company wrote the subcontractor's bond there involved.

Lennox Industries supplied materials to the subcontractor A & A, who failed to pay for them. In much the same manner as plaintiff in this case, Lennox, the supplier, sued A & A, the subcontractor, and its surety, American, and Brezina, the prime contractor, and its surety, General American. As in this case, Brezina, the prime contractor, filed a cross-claim against its subcontractor, A & A, and its surety, American, praying that any judgment recovered against Brezina be recovered from A & A and its surety.

The district court rendered judgment for Lennox against A & A, Brezina and its surety, but also granted judgment in favor of Brezina on its cross claim against A & A and its surety, American. American appealed.

The Court of Appeals affirmed. It held that the subcontractor who had agreed to "furnish all materials" did not do so when he failed to pay for them and that so far as liability under the bond was concerned "the conclusion is impelled that liability attached under the bond because A & A, the principal, failed to 'conform and comply with the terms and conditions of the contract'" (l.c. 607 of 295 F.2d).

Brezina Const. Co. announced and applied two rules of construction applicable to subcontractor's bonds furnished on a Miller Act project. The first rule was stated in footnote 6 on page 607 as follows:

> "The rule that the surety is a favorite of the law and that his bond should be strictly construed does not apply to surety companies organized for a profit, or to compensated surety."

The second rule of construction was stated in footnote 7 on page 607 as follows:

> "Under a recognized rule of construction, the instant bond must be viewed and interpreted in light of the provisions of the subcontract and the general contract, which by appropriate reference forms a part of the subcontract. Annotation 77 A.L.R. 46; 72 C.J.S. Principal & Surety, § 100, p. 579; 50 Am.Jur., Suretyship, § 31, p. 923. Consideration of the subcontract and instant bond, *in light of the general contract and statute,* clearly indicates Brezina's intention to fully protect itself to the extent that it was liable for payment of materials furnished to a subcontractor, and of A & A and its surety to accept this liability." [Emphasis ours].

Both rules are reiterated and applied to subcontractor's bonds on a Miller Act project in Home Indemnity Company v. F. H. Donovan Printing Co., 8 Cir. 1963, 325 F.2d 870, 874. In that case it was held:

> "It is a fundamental rule of construction that where the contract which is the subject of the performance bond is referred to in the latter, that the contract is to be regarded as a part of the undertaking of the surety under the bond. Massachusetts Bonding & Insurance Co. v. Feutz, 8 Cir., 182 F.2d 752, 756—757 (1950); United States v. Phoenix Indemnity Co., 4 Cir., 231 F.2d 573, 575 (1956). It is equally well-settled that where, as here, there is a compensated surety, the performance bond and the contract upon which it is based are construed most strongly against the surety and in favor of indemnity. American Casualty Co. of Reading, Pa. v. Brezina Const. Co., 8 Cir., 295 F.2d

603, 607, fn. 6 (1961); Massachusetts Bonding & Insurance Co. v. Feutz, supra, 182 F.2d [752] at 756."

[3] Brezina Const. Co., we think, makes quite clear that it applied the rules of decision developed under actions upon Miller Act prime contractors' bonds quite freely to an action which, on the facts, involved a subcontractor's bond. Judge Matthes definitively held that the subcontract and the subcontractor's bond both had to be considered "in light of the general contract and statute," which, of course, brought the Miller Act prime contractor bond cases into play. Such a view of our controlling court commands the conclusion that the fact that a subcontractor's bond, as factually distinguished from a statutory prime contractor's bond, may be involved in a particular case presents merely a factual difference but not a valid ground for legal distinction.[15]

We believe that Judge Matthes had this thought very much in mind when he said that a "contractor * * * does not comply * * * by simply placing the material on the ground and leaving it to the owner *or, in this case, the prime contractor* * * * to pay for it." (l.c. 607 of 295 F.2d). It would be an "owner" in the factual situation in which a prime contractor's bond is involved; it would be a "prime

15. If strict logic is insisted upon to support Judge Matthes' rationale, it could well be reasoned that cases concerning prime contractors and their bonds, which unquestionably must be read in light of the statute, are applicable to cases concerning subcontractors and their bonds, because it must also be said that the subcontracts are to be read in light of the prime contracts under which they are written and because that light requires not only the reading of the prime contract alone, but also a reading of the statute. All of this is to say that the parties to the subcontract and its bond on a government housing project intend that their legal rights and duties are to be determined by reading the subcontract and its bond in light of both the prime contract and the statute. The experience of the construction of government projects is consistent with this logical approach.

contractor" in the factual situation in which a subcontractor's bond is involved. In the latter factual situation, just as in the former, Brezina Const. Co. holds that the subcontract and its bond must be considered "in light of the general contract and statute."

The application of that rule of construction required the holding that it must be held that it was the intention of the subcontractor and of its surety to accept and bond the liability that the prime contractor intended to protect itself "to the extent that it [the prime contractor] was liable for payment of materials furnished to a subcontractor."

Allsop Lumber makes clear beyond further contention that the liability that D & L sought to protect itself against was the liability imposed by the Capehart Act, which has been held to confer substantive bond protection essentially similar to that afforded Miller Act suppliers. Brezina Const. Co. formulated rules of construction to be applied to subcontractor bonds on Miller Act projects that enables contractors, subcontractors, their suppliers and their sureties to understand that the extensive body of law applied to the construction of the bonds of prime contractors is to be applied to the bonds of subcontractors written to protect that liability in accordance with the well-known comment in MacEvoy and the earlier Supreme Court cases.

Allsop Lumber also expressed a desire to avoid the introduction of "further complications into an already too complicated area by the development of technical niceties of distinction" (page 452 of 336 F.2d). We need not develop again our reasons for seeking uniformity in connection with all the various problems growing out of the extensive Capehart litigation with which we have dealt. We did so fully in Travelers Indemnity (see particularly

pages 466—475 of 215 F.Supp.) and incorporate by this reference what we said there.

We not only believe those considerations are still valid but we also believe that the manner in which the parties conducted themselves in connection with the subcontractor's bond here involved can be explained only on the basis that they somehow instinctively knew that the obligation being accepted was in fact spelled out in the statute under which the Capehart Housing was authorized. The conduct of National Union in this case cannot be explained on any other reasonable basis.

[4, 5] We are convinced that because our controlling court has now so clearly identified the essential similarity between the substantive rights of all parties under the Capehart Act with the well understood rights of all parties under the Miller Act that we must once again make application not only of rules of decisions developed under the Miller Act to the bonds of a Capehart prime contractor, but that we must also apply to Capehart subcontractor's bonds the rules of construction that have been held to be applicable to subcontractor's bonds written on Miller Act bonded projects. We so hold.

Neither of the parties briefed this case on the theory that our consideration of the subcontract and the bond must be in the light of the prime contract and the Capehart Act. Nor have either of the parties discussed the question of whether the rules of construction established by Brezina Const. Co. for subcontractor's bonds on Miller Act projects should be applied to the subcontractor's bond involved in this case to the end that, to use Brezina Const. Co.'s language, the facts here involved "clearly indicates [D & L's] intention to fully protect itself to the extent that it was liable [under the Capehart Act] for payment

of materials furnished to a subcontractor, and of [Mojave] and its surety [National Union] to accept this liability."

National Union's arguments in this case proceed upon an unstated assumption that we ruled to be invalid in Travelers Indemnity. In that case, the surety companies argued that a prime contractor's bond under the Capehart Act was just an ordinary bond similar to those in use in any other private construction project (see other 466 et ff. of 215 F.Supp.). We rejected that argument and held that "all substantive provisions of the Miller Act and the Capehart Act would be read into all performance and payment bonds required in connection with any government housing project constructed under the Capehart Act" (l.c. 463 of 215 F.Supp.).[16]

National Union, in an obvious effort to avoid the implication of knowledge of the well-established payment procedures on all government construction contracts, which results from a reading of the subcontract and its bond in the light of the prime contract and the statute, contends that "the provisions of the subcontracts themselves * * * are alone controlling" (L—4, 53);[17] that the provisions in Art. IV (7) of the prime contract "* * * permitting progress payments based upon a percentage of the cost of 'uninstalled materials suitably stored on the mortgaged

16. We incorporated that holding by reference into this case in our ruling on plaintiff's motion for summary judgment. See page 914 of 217 F.Supp. That particular determination was approvingly noted by specific paraphrase on page 451 of the opinion of the Court of Appeals in Allsop Lumber.

17. References to "(L—4, 53)" indicate National Union's Requested Finding of Law L—4 and page 53 of the argument in support. References to "(F—1, 1)" are to National Union's Requested Findings of Fact and the appropriate page of the argument in support. A single page reference such as "(53)" refers to a portion of the argument in support of either a requested conclusion of law or finding of fact.

property in a manner acceptable to the Contractirg Officer' * * * are entirely inapplicable and uncontrolling on the issue whether payments by D & L to Mojave * * * were timely and proper" (L—4, 53); that the "payment provisions of the price contract were 'nowhere referred to or incorporated by reference in the subcontracts'" (L—4, 53); and that "there is no evidence that the surety ever even had available to it a copy of the prime contract" (53).

We have already found against National Union's argument that the prime contract was not incorporated and made a part of the subcontract. Exhibit AA, relating to the interior electrical bond, and Exhibit BB, relating to the exterior bond, both introduced by National Union itself, were admitted in evidence at the hearing (Tr. 33). Those exhibits show on their face that both the prime contract and the subcontract were attached to those exhibits and received by National Union.

The two provisions of the subcontracts upon which National Union attempts to base its ultimate material variance argument can not be read to mean what National Union now would say that they were intended to mean. Those two clauses are quoted in paragraph 32 of findings of fact above. National Union has requested that we find that the payments made to Mojave after the December telephone call were material departures from the terms of the subcontract because the payments were not for "material and labor in place," nor were the payments "based on actual progress," within the meaning of the subcontract's language (F—27, 29). National Union also requested that we conclude that the phrase "material and labor in place" cannot be said to "embrace materials merely on order by the subcontractor, or materials received and stored by it on the job-site" (L—5, 55). It is

also contended that the phrase "payment to be based on actual progress" of the subcontracts should be held to mean that "payments to the subcontractor were to have been based only upon work actually done, and materials actually used, in installations and structures" and that the "mere delivery of materials to the job-site, and stockpiling of materials thereon, was not 'actual progress', within the meaning of the phrase" (F—6, 59). And finally, National Union contends that "paragraph 9 of the subcontracts must be read as *requiring* not just permitting D & L to require, that Mojave submit releases, receipts or other vouchers evidencing payment for materials and labor before any part of the subcontract amounts could be made to it" (emphasis National Union's, 63).

[6] We expressly refuse to make the requested findings and reject National Union's argument as summarized in the preceding paragraph. An application of the rationale of Brezina Const. Co. requires that we not read those clauses in isolation but that they must be considered in light of the requirements of the prime contract, the statute authorizing the government construction and in light of the obvious intention of the parties at the time the bonds involved were written.

In so holding, we have not overlooked National Union's other arguments that are threaded throughout its request for findings and conclusions that run to the effect that D & L should be held to have known that the surety "would rely for its [i.e., National Union's] own protection upon the same strict compliance with all subcontract terms which was called for by the subcontracts themselves" (F—8, 8); that D & L, not National Union who bonded the subcontracts, was under duty to "take some sort of action, by executing progress payments to Mojave and materialmen jointly, or otherwise, to satisfy itself that

materials and labor furnished to Mojave were duly paid for" (L—9, 67); that D & L was "the only person capable of enforcing those protective measures" (67); that somehow, when a prime contractor requires a subcontractor to furnish a bond, and when such a bond is in fact furnished, the prime contractor has not legally protected himself in what MacEvoy called an "easy way," but that the prime contractor, under those factual circumstances, "becomes, in effect, a trustee for the surety" (71) and under some assumed duty to the subcontractor's surety to take the sort of protective measures for the surety's benefit that it would have been forced to take for its own protection only in the event the subcontractor should have been unable to furnish a bond; and finally, that "if D & L *had* followed closely the payment procedures it had itself written into the subcontracts * * * there would have been no unpaid materialmen, since Mojave would have been required itself to pay for materials before it requisitioned for payment from D & L on the basis of them" (87).[18]

All of National Union's arguments in the foregoing paragraph again attempt to avoid the legal consequences that follow from an application of the rule of construction that requires that the intention of the parties be determined from the subcontracts and their bonds read in the light of the prime contract and in the light of the statutes under which the government housing project was being built. We refuse to depart from that basic legal proposition and therefore expressly reject National Union's additional requests and the arguments made in their support.

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18. Exactly where Mojave was going to get the money except from a distribution of the prime contractor's draw is not suggested by National Union. In regard to the last clause of National Union's argument, it might just as well argue that if D & L, Mojave, and National Union had never heard of the Fort Leonard Wood Capehart project, the present lawsuit would not be pending in this Court.

We have outlined National Union's requests and have stated its supporting argument in detail in order to make clear for possible appellate review our total rejection of National Union's legal theories. For the purpose of further clarification, we find and conclude that the phrases "material and labor in place" and "based on actual progress," and the phrase conferring an optional right on D & L to demand payment evidence from Mojave, all as set forth in the subcontracts, must all be read in light of the prime contract and the statute under which the government housing was being constructed.

[7] When viewed in that light, it is clear to us that all parties, including National Union, must be held to have understood and intended that the payments would be made for material inventory as well as physical progress in accordance with established payment procedures on all government construction contracts; that payments in this particular case would be made by the prime contractor to its subcontractors in accordance with Art. IV (7) of the prime contract on "uninstalled acceptable materials suitably stored on the mortgage property in a manner acceptable to the Contracting Officer;" and that the specific obligation being bonded by National Union was Mojave's duty to pay for those materials, either with the money it received on its draw from the prime contractor (as is the usual case) or with other funds of its own.

It is also clear to us that all of the conferences, telephone calls, telegrams, and conversations concerning the payment of Mojave's requisitions for funds revolved around the fact that D & L was obviously unwilling to release substantial funds to Mojave until and unless Mojave furnished the bond required of it by the subcontract. It is equally clear to us that all parties must have fully understood each other on that score and that National

Union can not now be heard to say that it was not bonding the performance of a subcontract entered into on August 18, 1959, which, because of the amounts involved in the requisitions, it must be held to have known had been in the course of substantial performance for some considerable period of time.

Under the factual circumstances, we find that when National Union accepted the liability on Mojave's bonds it quite evidently elected to rely only upon its exceedingly inadequate investigation of Mojave's financial condition and the indemnity agreement it had obtained from Mojave's president and his wife on April 23, 1959 (Kaufman, Ex. K-2), and that it did not believe it needed to investigate further.

[8] Certainly the record is silent as to any real investigation, on job-site or otherwise, that National Union made concerning the progress of the work that had been performed on subcontracts it was bonding. And more important, the record is completely silent as to any precaution whatever that National Union took in regard to either investigating or working out the sort of practical arrangement that is usually worked out in similar factual situations, namely, that National Union would accept liability on the subcontractor's bond only if it were assured that the money being paid the subcontractor on the then current requisitions would be paid into a bank account jointly controlled by the subcontractor and the surety so that the surety would have an effective means of seeing that the payments made by the prime contractor to the subcontractor would in fact reach the material suppliers in order that there would be no breach of the bond. National Union failed to take the usual steps to protect itself at the time of its acceptance of bond liability; it cannot claim exoneration on its compensated surety obligation on the theory that

others failed to establish payment procedures that National Union did not see fit to establish for its own protection.

[9] Neither D & L, nor Mojave, nor was anyone else under any duty to protect National Union from either the negligence or the incompetency of its own agents. Nor can it fairly be said that this record supports any finding that National Union did in fact rely upon any term or phrase of the subcontracts. On the contrary, the record is quite clear that National Union fully understood that its security was "either the work performed to date or materials on site" (Tr. 42), and that it was a "normal condition * * * that a contractor would get paid for on-site material, materials which are stored on the job site" and that this is true "whether the contract is a Capehart or any other sort of contract" (Tr. 54).

To further sharpen our findings and conclusions we shall make the definitive determinations requested in subsection C of the final amended pre-trial order entitled "Issues of Fact and Contention of Parties." We shall thereafter state appropriate conclusions on the issues of law outlined in subsection D of that order entitled "Issues of Law."

[10] The following findings and conclusions are therefore keyed to the paragraph numbers of the final amended pre-trial order:[19]

"30 (a) The manner in which the prime contractor made periodic progress payments to Mojave did not

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19. We recognize that several of the following numbered paragraphs, duplicate particular findings and conclusions already made and stated. We believe, however, that the parties are entitled, for purposes of possible appellate review, to have the specific questions of fact and law presented to us by their stipulations and by pre-trial order answered in language appropriate to that agreed upon by them.

vary from the terms and conditions set forth in the subcontracting agreements in any material respect.

"(1) The parties contemplated, intended, and understood that payments would be made for materials inventoried on the construction site but not actually incorporated into the work;

"(2) Mojave was not required by D & L to, and did not, nor was D & L under any contractual or other legal duty to require that Mojave submit with its applications for payments releases, receipts, or other vouchers evidencing payment by Mojave for labor and material.

"(3) All payments were 'based on actual progress' within the meaning of that phrase as used in the subcontracts.

"(b) None of the payments materially affected the nature and/or extent of, or the risk involved in National Union's obligations on each of its bonds.

[11] "(c) Defendant National Union has not shown, nor does any evidence show that any prejudice resulted to it under all of the facts found herein.

"(d) National Union is not released from any of its liability on the bonds here involved.

"(e) The prime contractor's payments to Mojave were made with the knowledge and consent of National Union.

"31. We agree with D & L's contention that it is apparent from the above facts that no alleged alteration did materially affect the nature and/or extent of, or the risk involved in National Union's obligations on each of its bonds. We reject National's contention that the facts show that National was in fact deprived of security to which it was entitled under the terms of the subcontracts.

"32. We reject National Union's contention that as a matter of law it has no burden of proceeding with evidence of resultant prejudice."

Under the facts and applicable law as we have found it, it is unnecessary to reach National Union's contention that under California law, which it argues is applicable by reason of a provision in the subcontracts that provides that "this contract shall be interpreted pursuant to the laws of the State of California," the surety should be completely discharged under the operation of Section 2819 of the California Civil Code.[20]

Since we have found no material alteration occurred either in fact or in law, the question posed in paragraph 33 of the amended pre-trial order as to whether a discharge should be considered as complete or only *pro tanto* is academic. Our findings, of course, also made academic the question of law posed in paragraph 36(a) below as to whether California or Missouri law is controlling in regard to the interpretation of the subcontracts or the bonds securing their performance and other questions. We have found that we must consider both those instruments in the light of the prime contract and the statute.

[12] Continuing from the paragraphs of the amended pre-trial order, we find and conclude that:

"34. The facts show the knowledge and consent of National Union, through its agent, to the making of the challenged payments.

"35. The separate payment bonds sued upon were issued by National Union as a result of a mistake,

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20. The statute provides that: "A guarantor is exonerated * * * if by any act of the creditor, without the consent of the guarantor, the original obligation of the principal is altered in any respect, or the remedies or rights of the creditor against the principal, in respect thereto, are in any way impaired or suspended."

which should not be held to increase the limits of liability established by the performance bonds written on each subcontract in the full amount of the subcontract price.

* * * * * *

"36 (b) The prime contractor did not alter the terms of its subcontract in paying Mojave for material inventoried on the site and not actually incorporated in the work.

"(c) The prime contractor did not alter the terms of its subcontract in not requiring Mojave to submit with its applications for each payment releases, receipts, or other vouchers evidencing payment for materials and labor, or any additional evidence bearing on the right of Mojave to such payments.

"(d) The prime contractor did not alter the terms of its subcontract in regard to the 'based on actual progress' language used in the subcontracts.

"(e) Under the facts and applicable law, there were no alterations material to the nature and/or extent of, or the risk involved in, National Union's obligations on the bonds in question.

"(f) National Union would have had the burden of showing the fact and extent of any prejudice suffered by it as a result of any and all of the claimed alterations.

"(g) The question of whether National Union would be released from its obligations on any of the bonds, *in toto* or *pro tanto*, is not reached for the reasons stated elsewhere.

"(h) The question of whether Mojave had any obligation, when requesting that National Union issue the performance and payment bonds sued upon, or at any time thereafter, to inform National Union that a progress payment of $50,000.00 had already been made by D & L to Mojave, need not be determined because we find National Union either knew or should

have ascertained on its own behalf that fact before it accepted liability on the bonds it issued.

"(i) D & L did not, under any circumstance, have any obligation, when it inquired whether National Union had in fact issued the performance and payments bonds sued upon, or any time thereafter, to inform National Union that a progress payment of $50,000.00 had already been made by D & L to Mojave.

[13] "(j) D & L may assert all its rights against National Union under the payment bonds issued by it to secure payment to persons furnishing materials used in the subcontracts."

The other subparagraphs of paragraph 36, subparagraphs (k) through (o), inclusive, relate to questions that concern particular items of damage, including the question of whether attorney's fees for defending materialmen's suits and for prosecuting this cross-claim should be allowed D & L as damages under the bond. The briefs of the parties have injected some additional questions concerning damage into the case.

Before directing further proceedings, but without getting involved in specific dollar amounts of damages and their allocation, we think it will be helpful to make definitive rulings in regard to several of the contentions made by National Union in regard to the extent of its liability on the bonds. We believe that specific discussion of particular requests made by National Union in regard to damages will aid the parties in connection with their work on the form of the final judgment.

We expressly reject National Union's request that the $143,621.00 payments "be subtracted from the total damages" (L-16, 99 and L-17, 102).

We expressly reject National Union's request that we find that it can not be held liable "in an amount greater

than $20,625.00, the amount by which the subcontract prices agreed upon by D & L, on the one hand, and Modern and Carter, on the other [Modern and Carter were take-over contractors employed by D & L when National Union refused to take over completion of Mojave's defaulted contract] exceeded the amounts of the two Mojave subcontracts" (L-K, 103).

National Union, admittedly without supporting authority, suggests that the failure of Modern and Carter to complete within the amounts specified in their respective take-over contracts somehow excused National Union from its surety obligation that Mojave would "promptly make payment of all just claims for materials and labor supplied or performed in the prosecution and completion of the work to be done" (quoted from the payment bond), and its surety obligation that Mojave "shall well and truly perform and carry out the covenants, terms and conditions of said agreement" (quoted from the performance bond).

National Union seemingly was unfamiliar with the usual action and practice taken by surety companies in the event of default of their principal on a construction project, either government or private. National Union, however, concedes that it could have "undertaken completion" (103) and thus have maintained its own control of the completion costs.

[14] But National Union elected not to follow that course. It elected to rely upon the alleged defenses which we have refused to sustain, and, in effect, to leave D & L without any benefit of the protection of the bonds whatever. Finding itself now in a quite radical legal situation, National Union attempts to argue that D & L violated all sorts of legal duties allegedly owed National Union to have protected National Union's interests in a manner

more adequate than National Union could have protected itself. National Union argues that because D & L entered into take-over contracts for the same amount of money provided for in the original subcontracts that it [D & L] somehow elected to rely upon its contract rights against the take-over contractors, and therefore "put an end to any chain of causation stemming from Mojave's default, and thereby fixed the maximum damages for which the latter might be held accountable" (104). National Union attempts to press this argument to its logical extreme by even suggesting that if D & L were permitted to recover in accordance with the conditions of the bonds any recovery above the amount of the take-over contracts would "shift the burden of their [the take-over contractors] defaults to National [Union]" (104).

We reject National Union's arguments in their entirety. We hold that the amounts specified in the take-over contracts have absolutely no bearing on the completion costs of the subcontracts bonded by National Union and that such amounts have no relevancy whatever in the calculation of the amount of damages to be assessed on the bonds.

For similar reasons, we reject National Union's requested conclusion L-23 which suggests that "in calculating damages due D & L * * * National Union must be credited with the full amount of the unpaid subcontract price in each case—$261.627.00 in the case of the interior electrical subcontract, and $124,752.00 in the case of the exterior electrical subcontract, or a total under both subcontracts of $386,379.00" (L-23, 115). We hold that the only limitation on National Union's obligation is that set forth in the respective bonds executed to insure the performance of Mojave and the payment by it of all just claims, namely, $330,000.00 in the case of the interior electrical subcontract,

and $200,000.00 in the case of the exterior electrical subcontract.

There remains for discussion only the items of attorneys' fees, pre-judgment interest, the "managerial and administrative service" item, the allocation of the General Electric settlement, and an apparent misunderstanding concerning the right granted National Union to examine supporting data concerning certain completion cost items at the time of the hearing.

We had considerable to say about an aspect of attorneys' fees and interest in this general type of litigation in our decision in Triangle Electric. The situation presented on this branch of the case is a bit different than the narrow questions we ruled on summary judgment in regard to plaintiffs' claim.

We note, however, that in connection with at least the attorneys' fee item of damage on the exterior subcontract any decision in regard to that particular item might be moot in the event we should sustain, as we have, National Union's contention that the liability on that particular bond is not double the contract price, even though four, rather than two bonds were actually executed.

Because the same situation may well exist in regard to other items and because we are confident that counsel are more familiar with the dollar amounts of all items than we are, we have decided not to attempt any final assessment of damage in this opinion.

In order, however, that final judgment be entered promptly, we direct that counsel for D & L within ten (10) days prepare a final order in accordance with the factual and legal determinations made herein and submit the same to counsel for National Union for approval as

to form. If National Union's counsel are unable to agree with D & L's counsel on the form of final judgment within a period of five (5) days after submission to them, counsel for both parties shall immediately advise the Court so that further proceedings may be directed after conference. We again thank counsel for both parties for their continued assistance and cooperation.

John W. Oliver
District Judge

APPENDIX F

United States District Court for the
Western District of Missouri
Western Division

TRIANGLE ELECTRIC SUPPLY CO., INC.,
Plaintiff,

v.

MOJAVE ELECTRIC CO., et al.,
Defendants.

No. 12904

KOPPERS COMPANY, INC.,
Plaintiff,

v.

CONTINENTAL CASUALTY CO., INC., et al.,
Defendants and Third-Party Plaintiffs,

v.

NATIONAL UNION FIRE INSURANCE CO. OF PITTSBURGH, PA.,
Third-Party Defendant.

No. 13232

[Filed February 26, 1965]

SUPPLEMENTAL MEMORANDUM OPINION, SUPPLEMENTAL FINDINGS OF FACT AND SUPPLEMENTAL CONCLUSIONS OF LAW

SUPPLEMENTAL MEMORANDUM OPINION

In our memorandum opinion of October 5, 1964, now reported as Triangle Electric Supply Company v. Mojave Electric Company, W.D.Mo., 1964, 234 F. Supp. 293, we noted that at the time of the original submission of this branch of the case National Union suggested that various questions relating to the amount of damages be reserved in order to " 'allow the parties to consult with each other as to the amount of judgment, if any, after the Court has made its decision on the various issues raised by the requested Findings of Fact and Conclusions of Law' " as initially presented by the parties, (pages 296 of 234 F.Supp.). In accordance with that suggestion we did not rule specifically on the items of damage concerning attorneys' fees, pre-judgment interest, and other particular items of damages (page 316 of 234 F.Supp.).

Our order of October 5, 1964, therefore directed counsel for D & L to prepare a final order and to submit the same to counsel for National Union for approval. The parties, however, were unable to agree. We then directed the submission of additional suggested findings and conclusions, together with supporting briefs. We have studied those briefs and shall make additional findings and state additional conclusions in order that final judgment may be entered.

The latest briefs of the parties reveal that particular questions formerly in contest are no longer contested. We therefore note at the outset that "National Union concurs with D & L in its statement (Br. p. 2) that the legal principle applicable to the issues now remaining for decision will be the same no matter whether Missouri, California, or federal law is held to be controlling" (page 1 of National Union's Supplemental Suggestions). National Union also agrees that, on the facts, the bond limitations of both the exterior and interior bonds are exceeded by items of dam-

age as to which no dispute remains (page 2 of National Union's Supplemental Suggestions).

The area of conflict between the parties' present positions relates to the questions of whether attorneys' fees and pre-judgment interest may be included in the judgment in excess of the amount of the bonds involved. National Union contends generally that neither item of damage may be allowed because to do so would exceed the $200,000 provided in the exterior bond, and the $330,000 provided in the interior bond. National Union also argues that pre-judgment interest may not be recovered in any event because the damages were not "liquidated;" because no demand was made on the surety; and because, as already stated, the sums provided in the bonds have already been exhausted by the allowance of other items of damage.

National Union's factual assertion that no demand was ever made by D & L can not be sustained in light of paragraph 29(1) of the amended pre-trial order which stipulated that "due notice of said defaults by Mojave was given National by D & L and due demand was made that National assume the duties of Mojave under said subcontracts." That paragraph of the amended pre-trial order adds that "National refused to comply with said demand, however, claiming that it had been released from its obligations under said performance and payment bonds by virtue of the actions of D & L and Mojave above described."

There is no question but that the demand referred to in that agreed statement was made on April 4, 1960. Hence the basic question for decision reduces itself to the question of whether attorneys' fees and pre-judgment interest may be allowed as elements of damage over and above the amounts specified in the bonds.

We deal first with the question of attorneys' fees. In our memorandum of October 4, 1964, we noted that the situation presented by this branch of the case in regard to attorneys' fees and pre-judgment interest was a bit different than the narrow question we ruled on summary judgment on the first branch of this case on June 30, 1963, now reported as Triangle Electric Supply Co. v. Mojave Electric Co., W.D.Mo.1963, 217 F.Supp. 913.

Our memorandum opinion of June 20, 1963, did not reach or rule the question of whether attorneys' fees and pre-judgment interest might be recovered in a case where no agreement existed between the parties in regard to those particular items (page 914 of 217 F.Supp.). We did, however, hold that Illinois Surety Co. v. John Davis Co., 244 U.S. 376, 37 S.Ct. 614, 61 L.Ed. 1206 (1917), was a case that we would follow, in addition to United States for the Benefit and on Behalf of Sherman v. Carter, 353 U.S. 210, 77 S.Ct. 793, 1 L.Ed.2d 776 (1957).

The Court of Appeals, in affirming our order of June 20, 1963, agreed that Carter controlled the factual situation where the contract made express provision for the allowance of attorneys' fees and interest. While the Court of Appeals limited its holding to that particular factual situation, as we had, it nevertheless helpfully stated that "where there is no express contract for interest or attorneys' fees, it is necessary to look to state law to measure the extent of the subcontractor's obligation" (page 1013 of 332 F.2d). The Court of Appeals relied upon John Davis Co. and by footnote directed attention to cases from the 4th, 9th and 10th Circuits that had allowed interest or attorneys' fees on the basis of state law "in situations where no express contract relating thereto existed" (see cases cited in footnote 4 on page 1013 of 332 F.2d).

[1] The factual situation in regard to attorneys' fees and the factual situation in regard to pre-judgment interest on this branch of the case are different. In regard to attorneys' fees, Paragraph 36 of Exhibit D expressly provided that "in the event Contractor [D & L] engages the services of any attorneys for any action brought by either party on or under this contract, or by either party for its enforcement or in defending any action brought against the Contractor due to the fault of this Subcontractor, the Subcontractor agrees to pay reasonable attorneys' fees to the Contractor." That paragraph also provided that the "Subcontractor agrees to hold the Contractor harmless by reason of any damages incurred by Subcontractor through the fault of the Subcontractor to fully and efficiently perform his contract and pay such costs, expenses, damages and/or attorneys' fees which Contractor may incur by reason of failure of Subcontractor to fully and completely perform hereunder." No such agreement existed in regard to the payment of pre-judgment interest.

The basic rationale of our memorandum opinion of October 5, 1964, and our application of the rule of decision of our controlling court in American Casualty Co. of Reading, Pa. v. Brezina Const. Co., 8th Cir. 1961, 295 F.2d 603, requires that we now hold that the express contractual agreement covering attorneys' fees places that item of damage in the same category as the attorneys' fees involved in our memorandum opinion of June 20, 1963, and that inquiry into state law is unnecessary.

The parties are in agreement as to the amount of fees. Paragraph 18 of the amended pre-trial order states that "in the event the Court finds that attorneys' fees are recoverable by D & L on account of the prosecutions of the causes asserted by D & L against National, at the trial level, the parties have agreed that a reasonable attorney fee there-

for would be $25,000 * * *." In addition the parties agreed that attorneys' expenses incurred total $435.00. Accordingly, the judgment shall include a provision allowing attorneys' fees in the amount of $25,000 and expenses in the amount of $435.00.

[2] We turn now to the question of pre-judgment interest. As an introduction to that subject, it should be stated that the allowance of pre-judgment interest is actually an assessment of damage for delay in the payment of a contractual obligation and does not represent, in the true sense of the word, interest as understood in banking circles. Mr. Justice Stone makes this clear in Royal Indemnity Co. v. United States, 313 U.S. 289, 61 S.Ct. 995, 85 L.Ed. 1361 (1941). He there stated that "a suit upon a contractual obligation to pay money at a fixed or ascertainable time is a suit to recover damage for its breach, including both the principal amount and interest *by way of damage for delay in payment* of the principal after the due date" (pages 295-296, 61 S.Ct. page 997). Suits on bonds such as the bonds here involved seek to recover amounts that are due and owing by the particular bonding company that has contracted to pay on default of its principal.

The fundamental theory of the assessment of what is known as "pre-judgment" interest represents the imposition of legal compensation for the use of money wrongfully withheld from payment. As Mr. Justice Stone noted in Royal Indemnity Co., "the debtor has had the use of the money, of which its default has deprived the creditor," and "interest upon the principal sum from the date of default, at a fair rate, is therefore an approximate measure of damage for the delay in payment" (pages 296-297 of 313 U.S., page 998 of 61 S.Ct.).

United States v. Seaboard Surety Co., 2d Cir. 1964, 339 F.2d 1, is the most recent case applying the rationale of

Royal Indemnity Co. That case specifically notes that "interest in excess of the penal sum of the bond may be owing by the surety where the interest results from the surety's default and not the principal's." (pages 3-4 of 339 F.2d). That case directed the district court to increase the amount of interest owed by the surety to date back to the date "that demand was made on Surety for payment" (page 3 of 339 F.2d).

The recent Missouri case of Cannon v. Bingman, Springfield Ct.App. 1964, 383 S.W.2d 169, is consistent with the principles applied in the federal cases just cited. That case quotes with approval the modern rule concerning allowance of interest as stated by a New Jersey court: "'It should be borne in mind that the whole tendency of courts of law and courts of equity for a considerable period of time has been to break away from hard and fast rules and to charge and allow interest in accordance with principles of equity, in order to accomplish justice in each particular case'" (page 174 of 383 S.W.2d). That case expressly stated that "we do not wish to rest our decision upon any technical rules which have grown up involving interest" (page 174 of 383 S.W.2d).

In our memorandum opinion of October 5, 1964, we noted that the action taken by National Union "[left] D & L without any benefit of the protection of the bonds whatever" (page 316 of 234 F.Supp.). We also noted that National Union disregarded the usual action and practice taken by surety companies in the event of default of their principal on a construction job. The ultimate result of National Union's refusal to act meant that it had the use of the money involved in this litigation since the time it refused to comply with the demand it concedes D & L made upon it. It would therefore seem apparent that unless there is some compelling legal reason why pre-judgment interest should

not be included in the judgment, it is obvious that justice requires that it be included.

[3] The mere fact that the allowance of pre-judgment interest would exceed the amount of the bond is not a valid legal reason for its disallowance. The allowance of pre-judgment interest in Illinois Surety Co. v. John Davis Co., supra, did in fact exceed the amount of the bond but that fact did not deter Mr. Justice Brandeis in affirming the assessment of that item of damage. Judge Mack, in the Court of Appeals opinion in the John Davis Co. case, reported in 7 Cir., 226 F. 653, 662, held that the "failure of the surety to discharge its obligation * * * after proper demand or commencement of suit subjects it to the payment of interest." Mr. Justice Brandeis, in the opinion of the Supreme Court, held that even though "the aggregate liability on the claims exceeded the penalty, it [the surety] was properly held for an additional amount equal to interest from the commencement of the suit" (page 382 of 244 U.S., 37 S.Ct. page 617).

[4] The law of Missouri is consistent with the principles just stated. Gary Realty Co. v. Sweeney, (1929), 322 Mo. 450, 17 S.W.2d 505, and Maryland Casualty Co. v. Kansas City, Mo., 8th Cir. 1942, 128 F.2d 998, make clear that Missouri statutes applicable to what must be called, strictly speaking, "penal bonds," do not prohibit recovery of pre-judgment interest where the breach of a bond condition involves an obligation to pay money.

The Supreme Court of Missouri in the Gary Realty Co. case held that "our statute does not deny a recovery of interest in addition to the penalty of the bond, in cases where the action is brought for the breach of a condition *for the payment of money*, although such condition may be a collateral one" (page 510 of 17 S.W.2d, italics the court's).

That case also held that "defendant's refusal to pay after demand entitled plaintiff to interest from the date of such demand" on the theory that "a bond is a contract * * * and, being such, the statute allows interest on the amount due thereon after demand of payment" (page 510 of 17 S.W.2d). The Supreme Court of Missouri therefore affirmed the trial court which had allowed a recovery of pre-judgment interest "in addition to the penalty named in the bond" (page 509 of 17 S.W.2d).

In the Maryland Casualty Company case, the Court of Appeals for the Eighth Circuit followed Gary Realty Co. That case affirmed the action of then District Judge Collet who entered judgment "in excess of the face of [the] bond" (page 1005 of 128 F.2d 998).

The Court of Appeals in Maryland Casualty Co. expressly held that the fidelity bond there involved was not a "penal bond" subject to the Missouri statutes relating to such bonds. It is clear from what we said in our memorandum opinion of October 5, 1964, that we, in the same manner, do not view the bonds here involved as "penal bonds." We hold the bonds here involved must be considered as contracts which at least call for collateral conditions and undertakings not dissimilar to those involved in Gary Realty Co.

[5] Finding nothing in either the federal or state law that would prohibit the allowance of pre-judgment interest, we find and determine that such interest should be allowed as an item of damage for the delay in payment that National Union elected to cause and that pre-judgment interest should be allowed from the date of the demand admittedly made on April 4, 1960.

We therefore make further the following supplemental findings and state supplemental conclusions of law.

Supplemental Findings of Fact

10. Although not separately recoverable, by reason of the failure of National Union's principal, Mojave, to promptly pay all who furnished labor and material in the prosecution of the work of the exterior electrical subcontractor, D & L reasonably incurred expenses in the amount of $83,301.74 in resolving and satisfying claims of persons so furnishing.

11. The costs reasonably incurred by D & L in completing the work of the exterior electrical subcontract after National Union on April 4, 1960, refused to undertake its completion did exceed the face amount of that subcontract, $200,000.00, as the parties could upon that date reasonably have determined that they would.

12. Although not separately recoverable, by reason of the failure of National Union's principal, Mojave, to promptly pay all who furnished labor and material in the prosecution of the work of the interior electrical subcontract, D & L reasonably incurred expenses in the amount of $28,479.41 in resolving and satisfying claims of persons so furnishing.

13. The costs reasonably incurred by D & L in completing the work of the interior electrical subcontract after April 4, 1960, did exceed the face amount of this subcontract, $330,000.00, as the parties could upon that date have reasonably determined that they would.

14. Interest on $200,000.00 computed from the date of default and demand, April 4, 1960, at six per cent per annum to November 16, 1964, would amount to $55,487.80, and accumulates thereafter at a daily rate of $32.90. Interest on $330,000.00, computed for the same period and at the same rate, would amount to $91,455.00, and accumulate at $54.24 per day, a total interest to November 16, 1964, of $146,942.80 and $87.15 per day thereafter.

15. A reasonable attorneys' fee for the prosecution of the instant cross-claim through trial would be $25,000.00.

Supplemental Conclusions of Law

1. This Court is possessed of jurisdiction over the subject matter hereof and the parties hereto.

2. As a direct result of the breach of the conditions of the instant bonds, cross-claimants were damaged in the sum exceeding the face amounts of said bonds, $530,000.00, so that the obligees, herein identified as D & L Construction Company & Associates, are entitled to judgment against the obligor, National Union Fire Insurance Company of Pittsburgh, Pa., in said sum of $530,000.00.

3. In addition thereto such cross-claimants are entitled to recover as a part of such judgment interest upon such sum of $530,000.00 at the rate of six per cent per annum from the date not later than their demand upon cross-defendants, April 4, 1960.

4. In addition thereto, and not limited thereby, such cross-claimants are entitled to recover of such cross-defendant a reasonable attorneys' fee for the prosecution through trial of such cross-claim in the amount of $25,000.00, and expenses in the amount of $435.00.

5. Cross-claimants are entitled to judgment against cross-defendant National Union Fire Insurance Company of Pittsburgh, Pa., computed to November 16, 1964, in the sum of Seven Hundred Two Thousand Three Hundred Seventy-seven and 80/100 Dollars ($702,377.80), with interest thereon at the rate of six per cent per annum from the date hereof until fully satisfied and for their costs herein expended.

For purposes of the record, we expressly refuse to make the supplemental findings and conclusions most recently suggested by National Union.

Counsel for D & L will submit an appropriate final judgment within five (5) days.

It is so ordered.

John W. Oliver
District Judge

Kansas City, Missouri
February 26, 1965

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1965

No. 1149

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,
Petitioner,

vs.

D & L CONSTRUCTION CO. AND ASSOCIATES,
a Joint Venture,

AND

CONTINENTAL CASUALTY CO.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR RESPONDENT IN OPPOSITION

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OPINIONS BELOW

As noted in the petition, the opinion of the Court of Appeals is reported at 353 F.2d 196 (Appendix, p. 5a); The opinion of the district court at 234 F. Supp. 293 (Appendix, p. 25a).

JURISDICTION

Recognizing that under the cited statute, 28 U.S.C. 1254-(1), this court has the power to issue the requested writ before or after rendition of a final judgment, we question only whether the exercise of such power, admittedly possessed, should be considered at this stage of the proceedings. Petitioner in its jurisdictional statement argues that the decision below is so novel, important and erroneous as to justify an exception and the interlocutory review of a judgment, concededly non-final. Our argument directed thereto appears below.

QUESTION PRESENTED

Deeming petitioner's statement inaccurate, respondent suggests that the sole question presented by this case in its present posture is:

1. Was there evidence sufficient to support the trial court's findings of fact that the subsequent conduct of the parties did not so materially depart from the terms of their contract so as to support the petitioning defendant's sole defense, a "material alteration" discharging its obligations as surety, so as to justify the affirmance of those factual findings by the appellate court?

STATUTES INVOLVED

The statutes cited in the Petition (p. 4) are those involved should petitioner's statement of the case and the questions presented be accurate; none are involved in respondents' view.

STATEMENT

After the final adjudication of the claim of the original plaintiff,[1] there remained in the case but the respective cross-claims of the present petitioner and respondents. Respondents (the prime contractor referred to as "D & L") had cross-claimed against petitioner (surety for an electrical subcontractor, "Mojave") for damages suffered by them in completing the work of petitioner's principal. the defaulted subcontractor. As its defense petitioner claimed to have been discharged from all liability on its bonds, admittedly executed and delivered, by reason of claimed differences between the express terms of the subcontracts which it had bonded governing the manner in which periodic progress payments were to be made to the subcontractor during the course of construction and the subsequent conduct of the parties in the actual practice of the making of such payments.

The challenged payments were said to depart from the terms of the subcontract in two particulars: as to amount in that they included payment for materials delivered to and stored upon the construction site but not physically incorporated into buildings; as to time in that evidence of payment by the subcontractor for such materials was not required as a condition precedent to each payment.

As to this defense the findings of the trial court were that the manner in which the payments were made conformed with the recognized practices for this type of construction work (Nos. 29 to 33, Appendix pp. 32a to

---

1. Reported as *D & L Construction Co.* v. *Triangle Electric Supply Co.*, (8 Cir., 1964) 332 F.2d 1009.

35a); was that contemplated by the surety when it executed its bonds (No. 34, p. 35a); particularly as to the challenged payments (Nos. 36-41, pp. 36a to 37a) that (Appendix 64a *et seq.*):

> "30(a) The manner in which the prime contractor made periodic progress payments to Mojave did not vary from the terms and conditions set forth in the subcontracting agreements in any material respect.
>
> '(1) The parties contemplated, intended, and understood that payments would be made for materials inventoried on the construction site but not actually incorporated into the work;
>
> (2) Mojave was not required by D & L to, and did not, nor was D & L under any contractual or other legal duty to require that Mojave submit with its applications for payments releases, receipts, or other vouchers evidencing payment by Mojave for labor and material.
>
> (3) All payments were 'based on actual progress' within the meaning of that phrase as used in the subcontracts.'
>
> (b) None of the payments materially affected the nature and/or extent of, or the risk involved in National Union's obligations on each of its bonds.
>
> (c) Defendant National Union has not shown, nor does any evidence show that any prejudice resulted to it under all of the facts found herein.
>
> (d) National Union is not released from any of its liability on the bonds here involved.
>
> (e) The prime contractor's payments to Mojave were made with the knowledge and consent of National Union.
>
> **31. We agree with D & L's contention that it is apparent from the above facts that no alleged altera-**

> tion did materially affect the nature and/or extent of, or the risk involved in National Union's obligations on each of its bonds. We reject National's contention that the facts show that National was in fact deprived of security to which it was entitled under the terms of the subcontracts."

Concluding (Appendix, p. 48a *et seq.*) that its duty was to interpret the intent of the parties to the subcontract in view of all the surrounding facts and circumstances, the trial court made the ultimate finding (No. 42, Appendix p. 37a) that: 'The making of the above payments did not materially alter or affect the nature or extent of the obligations originally assumed by Mojave under the aforesaid subcontracts nor those assumed by National in executing the instant bonds." The trial court found (p. 66a) it "unnecessary to reach" and to be "academic" the questions posed by the parties as to the applicable law.

Upon petitioner's appeal the Court of Appeals for the Eighth Circuit disposed of the liability issue in one paragraph (Appendix, p. 13a) holding such findings to be supported by substantial evidence and, therefore, affirming.

The remaining portion (denominated B) of the opinion upon petitioner's appeal dealt with the proper assessment of damages (Appendix, pp. 14a to 21a). Because of error found in a failure to properly credit subcontract balances the cause was remanded to the trial court for "redetermination of the amount of damages due (respondents)."

ARGUMENT

Such is the state of the record and such are the issues upon which at this stage of the proceedings petitioner asks this court to interpose its review. We respectfully submit that, so understood, the judicial determinations which peti-

tioner asks this court to now review are important to no one other than the parties to this case. The case presents no issue other than whether two payments made in 1959 accorded with the particular intent of particular parties to a particular contract. It has no other importance. If the findings of the trial court on that issue were based upon substantial evidence they should, as they were, have been affirmed.

This case does *not,* as the petition would suggest, involve: The adjudication of any right or defense of the petitioning surety by "federal judge-made law" in recognition of any state law productive of any contrary result (Petition, "Questions Presented", No. 1); "The imposition of federal judge-made rules of decision" contrary to any such state law (ipse, No. 2); the creation of "novel and unprecedented federal rules of decision" opposed to any such state law (ipse, No. 3); the "incorporation by reference" of all terms and conditions of federal prime contracts into private subcontracts (ipse, No. 4); or the application by federal courts of a body of law other than that selected by parties to a subcontract (ipse, No. 6).

This case involves, all *dicta* aside, but one judicial function, but one principle of law, that all contracts, private or public, are to be interpreted in accord with the intent of the parties as such intent may be ascertained from all of the surrounding facts and circumstances. As to this particular contract the trial court painstakingly reviewed all of the evidence before it which would be of any assistance in determining that intent. This petitioner was intitled to contest in the appropriate appellate court the detailed findings made by the trier of the fact in interpreting the intent of the contracting parties. Those findings have been duly reviewed and by the appropriate court found to be correct and supported by substantial evidence.

We respectfully submit that that is all that this case is about.

I. THE REVIEW OF THE NON-FINAL JUDGMENT NOW SOUGHT WOULD NOT PRESENT ANY IMPORTANT QUESTION OF LAW, STATE OR FEDERAL.

The decisions below are neither wrong nor "wrong in a way that is destructive of the constitutional principles which control the interaction of state and federal laws in our complex federal system" (Petition, p. 18).

Bereft of an appealable issue, the petition would seek to raise the scepter of every issue in current vogue. While the petition (pp. 14-17) states "nine important reasons" why a writ of certiorari should be granted, none are present "in this case". The decisions below do not conflict with this court's decisions in *Erie R.R. Co.* v. *Tompkins*, 304 U.S. 64, or its progeny (No. 1). Neither the trial nor the appellate court ignored or misapplied the Rules of Decision Act, 28 U.S.C. 1652 (No. 2). The interpretation of the instant subcontract did not present an important, unsettled "continuing problem of the interaction of federal and state laws in our complex federal system" (No. 3). That interpretation was of "incalculable significance" only to the parties to this lawsuit and does not "directly affect the thousands of private transactions" nor "likely change the rules by which those transactions are planned and executed" (No. 4); That decision conflicts with no other decision of other federal courts in any circuit (No. 5). The rule that contracts are to be interpreted according to the intent of the parties rests upon ground firmer than legislative inactivity (No. 6). There is no conflict between the decisions below and that of this court in *Guerini Stone Co.* v. *Carlin Const. Co.*, 240 U.S. 264 (1915). This case does not present "a serious instance of improper administration"

of the *Erie* rule nor any sanctioning by the Court of Appeals of a departure "from the accepted and usual course of judicial proceedings" (Nos. 8, 9).

Whatever cases might have been cited in either of the opinions below, whatever *dicta* may be excerpted, this case presents to the trial court, to the appellate court, and to this Court but one question, "What was the intent of the parties to the instant subcontract?" After examining all of the evidence before it which could possibly have shed any light upon the ascertainment of that intent, the trial court made detailed findings of fact dispositive of that issue. Those findings were found by the appellate court to have been not only based upon substantial evidence but to be correct. Reading the challenged clauses of the subcontract not in isolation but "in light of the obvious intention of the parties at the time the bonds involved were written" (234 F. Supp. 293, 311), in the knowledge of the parties' knowledge of the "well established payment procedures on all government construction contracts" (l.c. 310), in the light of what the contracting parties were trying to accomplish—indemnity against the known liability of a prime contractor on a government construction project, noting that the instruments being bonded "specifically incorporated" all of the provisions of the prime contract (l.c. 306), the court interpreted the parties' expression of their obligation. Not, as petitioner would charge, incorporating all of the federal requirements *en masse* into the subcontract bonds, but reading those bonds in the light shed by those requirements. We simply cannot understand how that exercise of that judicial duty can be said to contravene any law, state or federal, pre or post-*Erie;* how it involves any "novel" or "unprecedented" question; why the exercise of that duty calls for the exercise of the power of this court to correct the improper administration of justice.

Exemplary of the real nature of the issue it may be noted that in the unpublished decision printed as an appendix to the brief for appellees below, we find that another trial court in another circuit has perceived the judicial duty to be the same as that below exercised and, without citation to any decision, state or federal, or discussion of any questions as to the choice of law, arrived at the same result upon the same facts (*United States for Use of Triangle Electric Co.* v. *D & L Const. Co., et al.*, U.S.D.C., N.Mex., 1/6/65, No. 4656, Brief for Appellees, Appendix, p. 1).

II. THE DECISIONS BELOW CONFLICT WITH NEITHER STATUTE NOR JUDICIAL DECISION.

A. Not with the Rules of Decision Act.

The first conflict which the petition would attempt to create (pp. 18-25) is with the Rules of Decision Act, 28 U.S.C. 1652.

In order for there to be a "conflict" with the law to which that statute might direct us, it would seem that there must first be a demonstration of a difference between the law of one jurisdiction and that of the other. Petitioner's position is that had the law of California been applied, a material alteration would have discharged its suretyship obligation *in toto*. Assuming *arguendo* such to be so, then there is nothing to indicate anything to the contrary in either opinion below. *Had there been a material alteration*, the extent of discharge would have been a material consideration. Having found that there was *no* material alteration, both courts found it unnecessary to pass upon any questions as to the extent of discharge. Whether the law of Missouri, California, or some federal law would in that event have been the proper jurisprudence to consult is, as the court noted, a moot question. The question which the court below was called upon to decide was the ascertainment of the intent of the parties, a ques-

tion of fact. We respectfully submit that that fact would have remained the fact whether the citations in the opinion had been to Missouri, California, or other courts of appeal.

B. Not Any Decision of This Court.

The second "conflict" is that said to exist between the opinion below and that of this Court in *Guerini Stone Co.* v. *Carlin Constr. Co.*, 240 U.S. 264 (1915), a conflict said to be so serious so as to call for the exercise of this court's power of control of judicial administration.

We can only reply that we can find no logical similarity or relevance in the discussion in *Guerini* of the attempt to create a non-existent termination clause to the problem in this case, the interpretation of a payment clause admittedly in the contract. Reading a subcontract "in the light of" a prime contract is considerably different than binding a subcontractor to each and every clause in the prime contract, clauses of which he may or may not have notice.

C. Nor Any Decision of Any Court, State or Federal.

The final effort is to create the necessary "conflict" between the decision below and that of another circuit. We know of no decision of any other circuit court of appeal interpreting the language of this subcontract. Petitioner cites *Carruth* v. *Standard Acc. Ins. Co.*, (5 Cir., 1964) 329 F.2d 690 and *Socony Vacuum Oil Co.* v. *Continental Cas. Co.*, (2 Cir., 1955) 219 F.2d 645. The former interprets the coverage of a subcontractor's bond, properly, by the applicable law of the forum; the latter sustains a common law action against a subcontract surety. Neither holds that a contract is not to be interpreted according to the intent of the parties. Unlike petitioner we are not shocked by the inattention of the courts below to such citations.

III. THE DECISION BELOW IS CORRECT IN ALL EVENTS.

We have heretofore noted that whatever the law may have been cited throughout either of the opinions below, the result reached was correct in all events. There is simply no need to consider questions concerning the extent of discharge if there has not in fact been an alteration which could give rise to discharge. The trial court found no material alteration; the appellate court affirmed that finding. We do not see how a review by this court of questions which might have arisen had there been a finding of alteration would do other than delay the administration of justice or in any wise affect the result which would ultimately be reached. The intent of the parties does not change with the jurisdiction.

CONCLUSION

We most respectfully submit that whether or not the payments which were challenged in the trial did accord with the intent of the parties to this particular subcontract is a question unique to the parties of this case and is not one of "such imperative public importance" as to justify the deviation from normal appellate processes contemplated by Rule 20 of this Court. Nor is it, assuming the judgment below to have been final, "an important question of federal law" which has not been, but should be, settled by this court, the resolution of which was "in any way in conflict with applicable decisions of this Court" nor "departed from the accepted and usual course of judicial proceedings" as to call for an exercise of this court's power of supervision under Rule 19.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Copy of the foregoing brief in opposition received this ..... day of April, 1966.

.....

DOUGLAS STRIPP

Attorney for Petitioner

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

1. On April 25, 1966, the Court announced its decision in *Wallis* v. *Pan American Petroleum Corp.*, No. 341, 34 U.S.L.Week 4373 (U.S. April 25, 1966), holding that federal courts adjudicating leasehold rights to oil rich

"mud lumps" in the Mississippi River should have applied Louisiana law rather than federal common law. The decision of the Fifth Circuit Court of Appeals holding otherwise was reversed.

This Court's ruling in the *Wallis* case requiring the application of state as opposed to federal common law directly applies to and governs the disposition of the present case.[1] Thus the Petition here affords the Court yet another opportunity to clarify an additional aspect of the continuing problem of the interaction of federal and state laws in the October, 1965 Term of Court—a term already marked by important and decisive rulings in this same area of the law.

As we show in our Petition, the issue of National's exoneration and discharge from liability under its subcontract bonds arises from an individually negotiated surety agreement between National and Mojave, the subcontractor. There has been no showing at any point in this ltiigation that the federal government has any interest direct or remote in the outcome of the dispute or that any federal program will be thereby affected. Petition, pp. 24-25, 30-32. The claims at issue in the courts below were not based upon any violation of federal statute, regulation or order, the subcontracts and bond were not governed or regulated by the Capehart Act, their validity was not in issue under that act or any other federal statute and the United States was not a party to the transaction in suit. Disregarding these factors the lower courts felt compelled to apply "federal common law" to the substantive issues in the case because of "the federal interest inherent in Capehart projects" (353 F.2d at 172; Petition, p. 7a), and the desire for "uniformity in connection with all the

1. *Wallis* and the Solicitor General's views on the choice of law question in that case were discussed at pages 25, 30-31 of the Petition.

various problems growing out of the extensive Capehart litigation". 234 F.Supp. at 309; Petition, p. 56a. Neither of the lower courts explained this "federal interest" or the reasons for "uniformity" in this case.

Certainly neither court demonstrated "a significant conflict between some federal policy or interest and the use of state law in the premises" which required that state law be disregarded in favor of an *ad hoc* rule created by the lower federal courts. *Wallis* v. *Pan American Petroleum Corp.*, 34 U.S.L.Week at 4374. Likewise neither court demonstrated a "significant threat to any identifiable federal policy or interest". *Ibid.* Nowhere in the opinions of the lower courts or in the briefs of Respondents was it suggested how use of state law on the questions before the courts might interfere with the policies underlying the Capehart Act, 42 U.S.C. § 1594 or the Miller Act, 40 U.S.C. §§ 270a and 270b. Those statutes "basically relate" to the rights of private persons *vis-á-vis* the Secretary of Defense or the contracting officer, and not, as here, to the right of private persons *inter sese*.[2]

The decision in *Wallis* emphasizes the aberrant character of the decision in the court of appeals; our Petition shows how this aberration introduces confusion and uncertainty into the planning and participation of private citizens in a federal program of vast dimensions. With these facts in mind this Court is respectfully urged to grant certiorari, to reverse summarily the decision of the Eighth Circuit Court of Appeals in the present case and to remand that case for proceedings not inconsistent with the opinions in *Wallis* and *United States* v. *Yazell*, 382 U.S. 341.

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2. See Comment, "The Competence of Federal Courts to Formulate Rules of Decision," 77 Harv.L.Rev. 1084, 1091 (1964) where the writer concluded that the reach of legislative policy under the Miller Act was not so extensive as to demonstrate a federal interest in the prime contractor's right of recovery against a subcontractor or supplier or in an interpretation of the subcontract on a Miller Act project.

2. Respondents argue at page 5 of their Brief that the trial court found it "unnecessary to reach" and to be "academic" the questions posed by the parties as to the applicable law. 234 F.Supp. at 314; Petition, p. 66a. This reconstruction of a portion of the district court's opinion lacks candor. That court made it clear in the preceding paragraph why it was "unnecessary to reach" the choice of law question:

> "Under the facts *and applicable law as we have found it*, it is unnecessary to reach National Union's contention that under California law, . . . the surety should be completely discharged under the operation of Section 2819 of the California Civil Code." (*Ibid;* emphasis supplied.)

And in the same paragraph of the district court's opinion from which Respondents drew excerpts, the district court said that, with respect to the interpretation of the subcontracts or the bonds securing their performance, "we have found that we must consider both these instruments in the light of the prime contract and the statute." *Ibid.* Thus the question of the application of state law became "academic" only because the district court had already determined that the law to be applied was "federal" law, that under this federal law the rights of the subcontractor's surety were to be measured by a statute and prime contract with which it had nothing to do,[3] and that so measured the Surety's rights were not "impaired" or "altered" by the prime contractor's acts and conduct.

Respondents thus miss the point, not only of the Petition but also of the opinions of the courts below. One

3. Nothing except in the Pickwickian sense that without the Capehart Act and the prime contract there would have been no project at Fort Leonard Wood and hence no subcontract for Petitioner to bond. See Comment, "The Competence of Federal Court to Formulate Rules of Decision," 77 Harv.L.Rev. 1084 at 1096 (1964).

might more aptly say that Respondents sidestep the point. Both lower courts met the issue more squarely and candidly. The court of appeals said at the very outset of its opinion that the body of law which governed the appeal must be determined before it could rule on the substantive legal issues. 353 F.2d 169 at 171; Petition, p. 7a. Likewise, the district court ruled that it would apply "the legal principle we first announced in *United States* v. *Travelers Indemnity Company* . . ." (234 F.Supp. 293 at 305; Petition, p. 48a) "that the rules of decision that will be applied to the factual situations involved in the various [Capehart Act] cases will be the rules of decision developed under the Heard and Miller Act decisions and that all substantive provisions of the Miller Act and the Capehart Act were to be read into Capehart Act bonds." *Ibid.* Thus it is absolutely clear that both lower courts determined "the intent of the parties" (as the Respondents emphasize), and whether there had been "a material variation" sufficient to discharge Petitioner, *only* in conformity with the federal law which those courts decided should apply. Indeed there can be no other explanation for the complete disregard of many provisions of the subcontract by which Petitioner's rights and duties should have been gauged. See pages 10-14 of the Petition.

We agree that this is a case of contract interpretation. The question which Respondents dodge, however, and which the Petition raises is whether the rules of contract interpretation which would ordinarily govern the dispute between the parties are to be abandoned in favor of rules of construction developed for the first time in this case under the aegis of some undefined federal common law.

3. Respondents likewise ignore the obvious impact of the lower court decisions on all transactions remotely connected with government procurement and construction; they

ignore the confusion and uncertainty which those decisions will generate. If the decisions below are allowed to stand, every subcontractor, materialman or supplier on any government project or in any government program may find that he can no longer rely on the express terms of his written subcontract or agreement to determine his relative rights and duties. Thus the fact that a prime contractor on a federal project may have dealings with a subcontractor, materialman or supplier, or the fact such persons receive instruction, information or guidance from the prime contractor or the mere fact that they are on the job will be sufficient under the lower courts' rulings to subject their rights *inter sese* to regulation under federal statutes and provisions of contracts between the prime contractor and the government. Such a far-fetched result is not justified by any statute involved in this case.[4]

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4. Compare *Fidelity & Deposit Co. of Maryland* v. *Harris*, 34 U.S.L.Week 2563 (9th Cir. 1966), refusing to hold that a lessor of equipment to a Miller Act subcontractor was within the coverage of that statute.

CONCLUSION

For the reasons stated in the Petition for Certiorari and in this Reply Brief, the Petition for Certiorari should be granted. Furthermore, in view of this Court's decision in *Wallis* v. *Pan American Petroleum Corp.*, we respectfully suggest that summary disposition is warranted. Certiorari should be granted, the decision of the Eighth Circuit Court of Appeals reversed and the case remanded for further proceedings consistent with the ruling there.

Respectfully submitted,

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